88-1066

Supreme Court, U.S.
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No.

In The Supreme Court of The United States
October Term 1988

ESTATE OF GEORGE JOHNSON, ELEANOR MADSEN, CARMEN COLON, CASIMIRA MACIAS, SOLEDAD FREGOSO, MANUEL COLON, HILDA VALDES, CARMEN REGALADO, AMERICA SUAREZ, FERDINAND KANGISER, MARIA ROMERO, RAFAEL MENDOZA, JOSE LUIZ CORONA, HERIBERTO PIZZARO, RAMON GONZALAS, AND GUILLERMINA OLIVARES,
For Themselves and all Participants in the Reliable Profit Sharing Plan Trust except CHARLES W. LEIGH AND ERVIN F. DUSEK, the Plaintiffs.

Petitioners

v.

CLYDE WILLIAM ENGLE, NATHAN DARDICK, RONALD ZUCKERMAN, LIBCO CORPORATION, TELCO MARKETING SERVICES, INC., TELVEST, INC., THE RELIABLE EMPLOYEES' PROFIT SHARING PLAN TRUST, AND NATIONAL BOULEVARD BANK OF CHICAGO, A National Banking Association.

Respondents

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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QUESTION PRESENTED

WHETHER, UNDER THE EMPLOYEE RETIREMENT INCOME SECURITY ACT, FIDUCIARIES AND PARTIES IN INTEREST WHICH ENGAGE IN PROHIBITED TRANSACTIONS WITH ASSETS OF A QUALIFIED EMPLOYEE PROFIT SHARING PLAN ARE ENTITLED TO RETAIN ALL THEIR PROFITS FROM THE PROHIBITED TRANSACTIONS, RATHER THAN TO DISGORGE THEM TO THE PLAN IN ORDER TO INSURE THE CONGRESSIONAL PURPOSES OF HONEST AND FAITHFUL MANAGEMENT OF QUALIFIED EMPLOYEE BENEFIT PLANS?

LIST OF PARTIES

The parties to the proceedings below were CHARLES W. LEIGH and ERVIN DUSEK, the Plaintiffs[1], participants having funds in the Reliable Manufacturing Corporation Employees' Profit Sharing Plan. The Petitioners before this Court are the INTERVENING PLAINTIFFS, individually and as representatives of the certified class of participants, having funds in the Reliable Manufacturing Corporation Employees' Profit Sharing Plan, except CHARLES W. LEIGH and ERVIN DUSEK, the Plaintiffs.

The respondents before this Court are all the defendants in the court below.

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[1] Plaintiffs did not pursue their appeal in the court below.

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TO THE UNITED STATES COURT OF APPEALS
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The Petitioners, Estate of George Johnson, et. al., etc., respectfully pray that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Seventh Circuit, entered in the above-entitled proceedings on September 21, 1988, as amended September 30, 1988.

OPINIONS BELOW

The opinion of the Court of Appeals for the Seventh Circuit is reported at 858 F.2d 361, and appears in the appendix hereto, p.1a. The Findings of Fact, Conclusions of Law and Judgment of the Northern District of Illinois (Duff, D.J.) is reported at 669 F.Supp. 1390 (N.D.Ill. 1987). It appears in the appendix hereto, p.21a. A memorandum and order of the Northern District of Illinois (Moran, D.J.) is reported at 619 F.Supp. 154 (N.D.111.,1985). It appears in the appendix hereto, p.79a. An unreported order of the Seventh Circuit entered May 30, 1985, appears in the appendix hereto, p.93a. The primary opinion of the Court of Appeals for the Seventh Circuit ("Leigh I") is reported at 727 F.2d 113, and appears in the appendix hereto, p.95a. A Memorandum, Findings of Fact, Conclusions of Law, and Judgment of the Northern District, entered November 18, 1982, is unreported. It appears in the appendix hereto, p.148a.

JURISDICTION

Invoking federal jurisdiction under 29 U.S.C. Section 1132, petitioners intervened in plaintiffs' action in the Northern District of Illinois. On November 18, 1982, the Northern District of Illinois entered judgment against petitioners from which a timely appeal was taken. On March 20, 1984, the Seventh Circuit vacated and remanded this judgment.

On August 27, 1987, the Northern District of Illinois entered findings of fact and conclusions of law in a memorandum decision and a judgment. Petitioners appealed to the Seventh Circuit which affirmed the Northern District of Illinois on September 21, 1988, as amended September 30, 1988. No Petition for Rehearing was sought.

The jurisdiction of this Court to review the judgment of the Seventh Circuit is invoked under 28 U.S.C. Section 1254(1).

STATUE INVOLVED

29 U.S.C. Section 1109 (a) Liability For Breach of Fiduciary Duty (a) Any person who is a fiduciary with respect to a plan who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by this subchapter shall be personally liable to make good to such plan any losses to the plan resulting from each such breach, and to restore to such plan any profits of such fiduciary which have been made through use of assets of the plan by the fiduciary, and shall be subject to such other equitable or remedial relief as the court may deem appropriate, including removal of such fiduciary. A fiduciary may also be removed for a violation of section 1111 of this title.

STATEMENT OF THE CASE

Petitioners are seventeen former employees of the Reliable Manufacturing Company having fully vested rights in the Reliable Profit Sharing Trust. Invoking federal jurisdiction pursuant to the Employee Retirement Income Security Act, 29 U.S.C. Section 1132, they obtained leave to intervene in a suit initiated by plaintiffs under the same federal statute, both individually and as representatives of a class of persons who had funds in the profit sharing plan when the company ceased doing business in February 1979. Petitioners sought to impose additional liability and to recover all respondents' profits and any losses to the trust from respondents' improper and unauthorized use of vested and non-forfeitable funds pursuant to 29 U.S.C. Section 1109(a).

The essential facts material to the consideration of the question presented are not in dispute. To be concise, the Reliable Trust was created by Reliable Manufacturing Company in 1968 as a qualified employees' profit sharing trust and became subject to the Employee Retirement Income Security Act of 1974. The plaintiffs were the trust administrators until September 15, 1977, when they were replaced by Reliable's Board of Directors, of which Clyde

William Engle was chairman, with Nathan Dardick and Ronald Zuckerman.[2] Until March 1978, all trust assets were held in the form of fixed income money market investments.

In late March 1978, at the same time other members of the "Engle group" were purchasing substantial amounts of stock in Berkeley Bio Medical, Inc. ("Berkeley"), Hickory Furniture Company ("Hickory"), and Outdoor Sports Industries, Inc. ("OSI"), Nathan Dardick used 30% of the trust's assets to purchase stock in the same companies.

Dardick's investments in Berkeley and OSI earned substantial profits for the trust of 66% and 141%, respectively. His investment in Hickory produced only a net profit of 4%, including a loss on one third of the shares he purchased. The trust's aggregate return on these three investments was 72%. Appendix 27a and 103a. Likewise, the profits of the Engle Group on its funds invested in Berkeley and OSI, before and after the trust investments were substantial. On October 7, 1980, the "Engle group" owned 52.8% of Hickory. Petitioners presented evidence in the Northern District of Illinois that the Engle Group earned a total profit on these three investments of $9,825,198.00. Record, PX 412, pages 21-24, 26-29; PX 258-260.

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[2] Plaintiffs, Charles Leigh and Ervin Dusek, the former owners of Reliable Manufacturing Company sold Reliable to Libco, a holding company substantially owned and controlled by Engle in April 1977. Dardick is an attorney who was retained as personal counsel to Engle in 1978 and 1979. He was also general counsel to Libco, Telco, Telvest, GSC, the Bank of Lincolnwood and Sierra, all of which are a group of individuals and business entities with close connections to Engle. Zuckerman was a board member and investment consultant to Libco. The Seventh Circuit on occasion referred to Engle, Libco, Telco, Telvest, Dardick and Zuckerman as the "the Engle group." because the complex network of legal and financial relationships among them was central to its decision in Leigh I. Appendix 96a-99a.

The case was tried to the Northern District Court and after an extended bench trial, the Court (Leighton, D.J.) entered 23 pages of findings of fact and conclusions of law holding that Engle and Libco were not fiduciaries, that Dardick's investments were prudent, that the plan had sustained no loss or damage as a result of the plan investments made by Dardick, that the plan assets were used exclusively in petitioners' interest, that the plan trustee and administrators acted properly and reasonably in the partial termination of the plan, that any delay in distributing benefits was due to Reliable's bankruptcy proceedings, litigiousness, and the emotional involvement of plaintiffs' lawyer, that respondents' profits were made through the use of their own assets and no basis exists on which to require them to surrender their profits, Dardick and Zuckerman did not engage in prohibited transactions nor breach their duty to the plan, Telco and Telvest are "parties in interest", and ERISA creates no cause of action where the plan was not damaged.

The Seventh Circuit vacated and remanded this case, observing in its primary opinion "Leigh I", "The heart of the case is a dispute over how ERISA governs the actions of plan administrators and other fiduciaries with respect to investment activities in contests for corporate control." Appendix 96a. It decided that Dardick's investments of trust assets in target corporations in order to assist Engle and Libco in their quest for corporate control of a "control premium" were prohibited transactions in violation of Section 1106(a)(1)(D). The timing of the trust purchases of Berkeley stock in relation to other actions of the "Engle group shows that the trust assets were not used exclusively to further the interests of the trust beneficiaries. In particular, although the Engle group faced the danger of being "locked-in" as minority shareholders under hostile management in late February 1978, Engle increased his investment and purchased additional shares. Meanwhile, Dardick invested the trust's assets in the same company

making the Reliable Trust one of the minority shareholders. In June 1978, the Engle Group reached a settlement of its control contest, and Dardick sold the Reliable Trust shares as part of the settlement which called for the payment of a substantial premium.

The Reliable Trust investments in OSI showed a similar pattern. Dardick made the trust investment very early in the struggle for control of OSI. Throughout the period of purchases by the Engle Group and its fight for control of OSI, the Reliable Trust held its investment, even after Reliable's bankruptcy and the termination of its profit sharing plan trust. Throughout this period, Dardick was forcing OSI's management to yield control or to purchase the Engle group's shares at a premium. Ultimately, the trust's shares were sold for an enormous profit.

This similar pattern again was displayed in Hickory, although Hickory management decided not to resist the Engle group's efforts to gain its control. Dardick made and held the trust's investment until it became clear that the Engle group would be successful in its acquistion efforts. After it was clear that the Engle group would succeed, the trust's shares were sold at a low point in the market for a net profit of 4%, including a loss on one-third of the shares it purchased.

Concluding that Dardick and Zuckerman violated their fiduciary duties under Section 404(a), Section 406(a)(l)(D) and Section 406(b)(l) of ERISA by their investments in the Engle Group's takeover targets, the Seventh Circuit considered the liability of Engle and Libco. Engle and Libco were fiduciaries with respect to the selection and retention of Dardick and Zuckerman. Finding that their fiduciary duty extended to the trust investments, the Seventh Circuit remanded for the Northern District to determine whether Engle and Libco fulfilled their duties, reasonably and prudently in light of their knowledge that Dardick and Zuckerman faced conflicting loyalties with respect to the

trust's investments in the target companies. The Seventh Circuit held petitioners did not prevail on the merits against Telco and Telvest, the parties in interest, whose interests Dardick aided by the plan investments.

The Seventh Circuit also considered the Northern District's inconsistent findings of fact and conclusions of law pertaining to termination of the Reliable Trust. It vacated and remanded the issue of when the Reliable Trust terminated and whether respondents violated their fiduciary duties regarding termination and by delaying distribution of the plan assets while seeking to make distribution contingent on release from liability in this lawsuit.

It held that the respondent fiduciaries Dardick and Zuckerman breached their fiduciary duties and engaged in prohibited transactions and that petitioners had not prevailed on the merits against Telco and Telvest. The parties in interest. The Seventh Circuit remanded to the Northern District the formidable task of finding an appropriate measure of damages, if any. In doing so, the Seventh Circuit observed that petitioners contention, that they are entitled to all profits of the respondents in their own investments in Berkeley, OSI and Hickory, reaches too far. Section 1109, it held requires only all profits "made through use of assets of the plan" in order to establish a causal connection between the use of the plan assets and respondents' profits, if any. Since the trust investments in the target companies relative to respondents' investments are relatively small, the Seventh Circuit expressed its concern that were petitioners to recover all respondents' profits, the recovery could double or triple the size of the trust. Further, since ERISA is silent on how profits should be apportioned, the Seventh Circuit established a legal standard analogous to the apportionment of a copyright infringer's profits. With respect to the issue of burden of proof in such apportionment cases, this case was similar

to the common law problem in which a trustee commingles trust assets with his or her own so that it is difficult to discern which property and profits belong to whom.

Upon remand, arguments ensued on the legal standard that the Court of Appeals intended as the applicable standard since, it had referred to disgorgement as one remedy that Congress had intended. Appendix 110a. A petition to recall the mandate was denied and on June 27, 1985, the Northern District expressed the view urged by petitioners. Appendix 88a.

After concluding the remand trial of "Leigh I" the Northern District held that Engle and Libco violated their fiduciary duties only with respect to the trust investments and not with respect to delaying distribution of the trust assets. The Reliable Trust terminated on March 1, 1979, the date petitioners were layed off. Since Dardick and Zuckerman made distributions of trust assets in 1980 of approximately $1,000,000.00, the Northern District ruled that under the trust instruments there had been no delayed distribution of trust benefits. Likewise, the Northern District ruled that complete distribution of trust assets was not required since, Dardick and Zuckerman were entitled to retain trust assets in order to reimburse themselves for the expenses of this litigation.

The Northern District resolved the issue of respondents' profits against petitioners by reasoning that in order to avoid disgorgement of part of its profits, the respondents had to show that they did not result from misuse of trust assets. According to its analysis of the evidence, respondents met this burden and respondents were entitled to retain all their profits. The Northern District further held that respondents had caused a loss with respect to the Reliable Trust's Hickory investment and awarded the trust $6,704.00. A fee award was adjudged against respondents in part to sanction respondents for the prohibited

transactions and respondents were awarded fees pursuant to the Reliable Trust instruments.

On appeal, petitioners urged the Seventh Circuit to hold that the Northern District did not follow its mandate with respect to respondents' profits. Affirming the Northern District, the Seventh Circuit found that Judge Duff did an admirable job with the damage calculation which it called a formidable task. Petitioners claim that all or most of the respondents' profits from its investments in the three companies were attributable to the prohibited transactions and mismanagement of trust assets was rejected on the basis of Leigh I since it reaches too far. The Seventh Circuit's holding is that ERISA Section 1109 only allows recovery "where there is a causal conection between the use of the plan's assets and the profits made by fiduciaries on the investment of their own assets" regardless of respondents' prohibited transactions; and, given the investments' excellent returns and the miniscule percentage of the respondent's total investment made up of trust assets, petitioners are in no way entitled to that windfall since it results from respondents' own efforts.

In arriving at its holding, the Seventh Circuit agreed with the Northern District's determination that Dardick and Zuckerman did not have the potential to undermine the Engle Group's settlement in Berkeley, and respondents profits in OSI and in Hickory likewise were earned only through respondents' large investment and by their efforts. It therefore affirmed the Northern District, noting that while the fiduciaries did not err slightly in their attempt to create a proper portfolio – rather they simply made no such attempt – and, that while there is no way to overdeter such conduct, no matter how profitable the end result, the petitioners' appeal on damages lacked merit.

REASONS FOR GRANTING THE WRIT

I. THE SEVENTH CIRCUIT DECISION AFFIRMING THE DENIAL OF REMEDIAL RELIEF TO ERISA PLAN BENEFICIARIES FROM PROHIBITED TRANSACTIONS IS AN IMPORTANT FEDERAL QUESTION WHICH HAS NOT BEEN SETTLED BY THIS COURT BUT WHICH IS PROBABLY IN CONFLICT WITH EXISTING APPLICABLE DECISIONS OF THIS COURT

Review of the lower court's ruling affirming the Northern District's denial of remedial relief from prohibited transactions is essential because of the lower court's finding of prohibited transactions by the plan fiduciaries. The decision involves an important federal question which has not been settled. *Massachusetts Mutual Life Insurance Company v. Russell, 473 U.S. 134, 105 S.Ct. 3085, 87 L.Ed 2d 96 (1985).* This Court specifically left open the type of questions presented by the lower court's decision in this case. There the questions concerned, the extent to which Section 1109(a) allows extra-contractual compensatory or punitive damages to the plan. In the lower court's ruling affirming the Northern District's decision, one of the questions raised concerns its finding of prohibited transactions without disgorgement of all profits and restoration to such plan of all such profits of the fiduciary. That result thereby raises a question unsettled by this Court which is whether the appropriate interpretation and application of other equitable relief expressed in Section 1109(a) requires disgorgement of respondents' profits in order to effectuate the purposes of ERISA.

The Northern District's opinion, as affirmed by the lower court, squarely rejects any basis for punitive damages in its interpretation of Section 1109(a). Moreover, it also rejects "such other equitable or remedial relief as the court may deem appropriate", specifically provided by Section

1109(a) as the basis for disgorgement of profits. These two remedies of punitive damages and other equitable or remedial relief possess a common attribute but exist for different purposes. Punitive damages deter and punish. *Sommers Drug Stores v. Corrigan Enterprises, Inc., 793 F.2d 1456, 1463 (5th Cir. 1986), cert. den. 107 S.Ct. 1298.* Disgorgement of profits, as other equitable or remedial relief deters and restores profits of the breaching fiduciary to the plan that must be appropriately restored in order that the purposes of ERISA remain vital. The lower court's engrafting of a concept of factual causation, and not legal causation, onto its finding of prohibited transactions makes the result that is reached in this case probably in conflict with existing applicable decisions of this Court. This is because the Northern District predicated its findings and conclusions upon the factual causation standard from copyright law that the Seventh Circuit first established by its mandate in Leigh I, and not upon the legal causation standard of accepted trust law that follows the *per se* type of finding of 1106(a)(1)(D) liability made by the Seventh Circuit.

The decisions of this Court teach an application of the standard of legal causation that repeatedly rejects factual causation when a breach of fiduciary duty is found to exist. *Magruder v. Drury, 235 U.S. 106, 35 S.Ct. 77, 59 L.Ed. 151 (1914)* holds a trustee can make no profit out of his trust regardless of whether the trust benefits or loses. This duty it was found springs from the trustee's duty and his relationship to the estate or trust or, as here, the Plan. *Mosser v. Darrow, 341 U.S. 267, 71 S.Ct. 680, 95 L.Ed 927 (1951)* reversed the Seventh Circuit and surcharged Darrow when he authorized his appointees and subordinates to trade and buy up bonds of debtor subsidiaries. It rejected the Seventh Circuit's reasoning that the surcharge created a very heavy liability upon a man who enjoyed no personal profit and that Darrow's breach of duty must be condoned so as not to strike terror into mankind. Given the effective

ways in which a trustee may effectively protect himself and further his recourse to the courts for instructions, this Court held it was appropriate to surcharge such misuse and mismanagement of one's trust. *Snepp v. U.S.. 444 U.S. 507, 100 S.Ct. 763, 62 L.Ed 2d 704 (1980)* reversed a lower court, finding that a constructive trust and disgorgement were required and appropriate where the fiduciary employee failed to obtain a review of confidential and classified material prior to publication.

The meaning of appropriateness found in this Court's decisions when used by this Court teaches lawyers and federal courts that the word has no relationship to the facts giving rise to the breach of duty except one, and that is that there was a breach of the fiduciary's duty. The only relevant fact is whether a breach of duty occurred and whether the public purposes embodied in the applicable law should be enforced. *Porter v. Warner, 328 U.S. 395, 400, 66 S.Ct. 1086, 90 L.Ed. 1332 (1945).* The lower court twice found respondents engaged in prohibited transactions; yet, it affirmed the denial of the disgorgement of the breaching fiduciaries' profits over a misplaced concern that the plan would recover a "windfall" in the event disgorgement was allowed.

The actual conflict with decisions of this Court arise from the engrafting into Section 1109(a), the factual causation standard of copyright law as the means by which the Northern District had to address the prohibited transaction. In doing this the remedial purposes of ERISA to correct the prohibited transaction were placed in jeopardy. The lower court probably misunderstood the language of Section 1109(a) "and shall be subject to such other equitable or remedial relief as the court may deem appropriate, ..." Contrary to its opinon, ERISA is not silent with respect to the remedy for prohibited transactions. Nor, should the lower court's decision affirming the Northern District provide no remedy and thereby conflict

with existing applicable decisions of this Court. The fact that this Court has never settled the full extent of Section 1109(a) and the probable existence of conflict with applicable decisions of this Court are important reasons to grant certiorari to the Seventh Circuit.

II. THE SEVENTH CIRCUIT DECISION NARROWLY INTERPRETING AND CONSTRUING ERISA SECTION 1109(a) TO PRECLUDE DISGORGEMENT OF PROHIBITED TRANSACTION PROFITS HOLDS IMPORTANT IMPLICATIONS FOR EMPLOYEE BENEFIT PLANS NEVER INTENDED BY CONGRESS AND IN CONFLICT WITH PRIOR TRUST LAW

Unless reversed, the lower court's narrow construction of Section 1109(a) has significant and adverse implications both for the proper administration of qualified employee benefit plans and the federal courts. As observed by the lower court in Leigh I, benefit plans control and enormous pool of capital with extensive investments in securities (Leigh I, at 132, 727 F2d.) Today, "insider trading" by a well meaning fiduciary seeking to maximize the plan's investment portfolio is but one further current concern in the financial markets that easily impacts upon administration of benefit plan assets. The "Engle group" type of corporate raider is another concern that results from the lower court decision. *See, Sandoval* v. *Simmons,* 622 F.Supp. 1174 (D.C.Ill. 1985). Both inside traders and Engle group type corporate raiders may even be honest but imprudent, dishonest but prudent, or dishonest and imprudent. In all instances under the lower court's rationale, the criteria for disgorgement is not the prohibited transactions; or other breach of duty, it is whether there is a loss to the trust. See *Brock v. Robbins, 830 F.2d 640 (7 Cir. 1987).* The apparent but erroneous theory is that "risk of harm" to the trust by the trustee pales in significance to whether there is an actual loss. If there is an actual loss, the loss

must be made up under Section 1109(a). If the fiduciary obtains profits from use of the trust assets, he must restore them. This much is expressly provided by Section 1109(a). However, under the lower court's decision, so long as the plan sustains no loss regardless of the prohibited transactions or profit earned the plan has no remedy. The decision is plainly wrong. It is not and never has been the teaching of this Court's decisions that the loss or gain by the plan is the "linchpin" for relief against a breaching fiduciary.

Moreover, unless reversed the lower court's opinion either portends a move away from traditional trust law which is important to this Court's supervisory power of federal courts; or, it is likely to create conflicts among the circuits over the appropriate interpretation to be given "other equitable relief." The lower court's decision unnecessarily creates a "formidable task" for the federal courts. No federal appellate court has ever applied copyright law concepts of profit attribution to trust law or fiduciary relations seeking to halt breaches of fiduciary duty. Now, however, unless reversed other federal courts may attempt to likewise engraft onto ERISA copyright law concepts of attribution that Congress had since eliminated from copyright law. It is plain this "formidable task" and concern about "windfalls" is misdirected because disgorgement is not punitive damages.

As an initial matter there is no congressional debate to support the lower court's narrow interpretation of Section 1109(a). That section follows the statutory codification of fiduciary duty, a co-fiduciary's duty and enumerated prohibited transactions. It is not intentionally obscure. Unless the lower court's decision is reversed however dishonest or imprudent fiduciaries of every variety are now emboldened to argue with ERISA beneficiaries in the federal courts, if necessary for even ten years, that "good faith", "windfall", "fairness", "no plan losses", "distribution of over one million dollars", and "modern portfolio

and investment strategy" allow them profits from prohibited transactions. The entire concern of Congress expressed for preventing misuse and mismanagement to which this Court referred in *Massachusetts Mutual Life Insurance Company v. Russell, supra, fn 12* is nullified and held for naught for petitioners and all ERISA beneficiaries.

Another important implication arising from the lower court's decision is that for years in cases involving security law violations, disgorgement has been applied to "insider" type cases. The reason is the judiciary seeks to discourge insider trading. *See Securities and Exchange Commission v. Shapiro, 494 F.2d 1301, 1309 (2 Cir. 1974); Securities and Exchange Commission v. Texas Gulf Sulphur Co., 446 F.2d 1301, 1307-1308 (2 Cir. 1971). In Janigan v. Taylor, 344 F.2d 781, 786 (1 Cir. 1965),* the appellate court stated the position desired by the Congress in ERISA: "It is more appropriate to give the defrauded party the benefit even of windfalls than to let the fraudulent party keep them. . . . It is simple equity that a wrongdoer should disgorge his fraudulent enrichment." Since, this Court has shown no lessening of the importance of disgorgement in security law cases, the lower court in this case should be reversed so that ERISA remains vital and effective.

Congress expressly intended to eliminate the "great personal tragedy" experienced by employees promised a retirement benefit by their employer, but which is lost when the plan is terminated; *Nachman Corporation v. Pension Benefit Guaranty Corporation, 446 U.S. 359, 374, 100 S.Ct. 1723, 64 L.Ed 2d 354 (1980)* or, as petitioners experienced, when Reliable Manufacturing Corporation was shut down by respondents who were engaged in three corporate take over fights involving prohibited transactions. To avoid "great personal tragedy", ERISA even insulates the fiduciary from potential conflicts. *N.L.R.B v. Amax Coal Company, 453 U.S. 322, 333, 101 S.Ct. 2789, 69 L.Ed 2d*

672 (1981). Now, unless reversed, the lower court's decision requires federal district courts throughout the midwest to consider loss to the plan rather than prohibited transactions, obviating the last part of Section 1109(a) which Congress intended to be read and understood as the basis for the equitable remedy of disgorgement. ERISA intentionally incorporated the prophylactic concept of disgorgement for its strict, and even "draconian", effect. Bogert, *Trusts and Trustees*. Section 543 at page 480 (2d ed. 1960) states:

> "The principal object of the administration of the rule is preventive, that is, to make the disobedience of the trustee to the rule so prejudicial to him that he and all other trustees will be induced to keep away from disloyal transactions in the future."

A further and most unwanted implication of the lower court's decision and narrow interpretation of Section 1109a is that the federal courts are now empowered to accept explanations and excuses for the breach of fiduciary duty that were not and have not been accepted in such courts. *In re Beck Industries, Inc. v. Kirschenbaum, 605 F.2d 624, 636-637 (2 Cir. 1979)* the appellate court observed what petitioners urged in the Northern District, namely:

> "It is simply impossible to say that the price to be received by the estate is what it would have been if Ross had not entered into the JVA and concealed Butler's role. Courts do not take kindly to arguments by fiduciaries who have breached their obligations that, if they had not done this, everything would have been the same."

It was this argument which the lower court approved in petitioners' case. As a result, respondents are found to have engaged in prohibited transactions and have been rewarded with nine million dollars. The importance of this unwanted implication from this lower court decision is that it is profitable to breach fiduciary duty and to engage in

prohibited transactions so long as there is some profit to the plan. Another important implication from the lower court is that prohibited transactions that enrich a benefit plan require no sanction. The breaching fiduciary must not be allowed to retain the profits which the finding of a prohibited transaction have produced. Congress never intended to reward a fiduciary that gambles with trust assets (by engaging in a prohibited transaction) and wins himself a profit on his investment and on the plan assets (there is no harm to the trust) or be entitled to retain his profit because the result would have been the same had he not used trust assets. The focus of Section 1109(a) is intentionally not on loss or gain to the plan. *Magruder v. Drury, supra, at 119-120.* It is on preventing "great personal tragedy." *Nachman Corporation v. Pension Benefit Guaranty Corporation, 446 U.S. 359, 100 S.Ct. 1723, 64 l.Ed. 354, (1980).* It must be on preventing misuse and mismanagement of plan assets which this Court observed in *Massachusetts Mutual Life Insurance Company v. Russell, supra.* The focus of Section 1109(a) must never be left on a factual determination that is similar to prior copyright law where the lower court's decision rests.

The lower court's interpretation of ERISA as silent after its finding that respondents had engaged in three prohibited transactions raises important implications for benefit plans never intended by Congress. The implication is that the lower court and thereby all appellate courts that are pursuaded to follow the lower court, are too easily mistaking punitive damages for disgorgement–or a legal remedy for the equitable remedy. It is true in law cases, punitive damages serve only to punish and deter and are generally seen as a windfall to plaintiffs, who are entitled to receive full compensation for their injuries—but no more. *Smith v. Wade, 461 U.S. 30, 59; 103 S.Ct. 1625, 75 L.Ed. 2d 632 (1983)* (Rehnquist, J., dissenting) Yet, it is not punitive damages that petitioners specifically sought in their complaint. What was sought is the deterrent effect

of punitive damages or "other equitable relief" that Congress intended. Disgorgement of respondents' profits from admitted prohibited transactions is not punitive damages. The benefit served by inflicting this risk upon breaching fiduciaries is tailored to deter those who would place the making of risky profit upon the backs of employees who work diligently for the day of retirement. The remedy unlike punitive damages reaches only funds attributable to the breach, it cannot saddle respondents with exemplary damages out of all proportion to respondents' gain. The decision of the lower court has deprived petitioners of this equitable and effective remedy for the plan and it has denied to pensioners all over America the appropriate remedy that Congress intended.

Accordingly, the availability of disgorgement as a remedy for prohibited transactions pursuant to Section 1109(a) is in need of urgent clarification by this Court.

CONCLUSION

For the foregoing reasons, a writ of certiorari should issue to review the judgment and opinion of the Court of Appeals for the Seventh Circuit.

Respectfully submitted,

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December 20, 1988

88-1066

Supreme Court, U.S.
FILED
DEC 20 1988
JOSEPH F. SPANIOL, JR.
CLERK

No.

In The Supreme Court of The United States
October Term 1988

ESTATE OF GEORGE JOHNSON, ELEANOR MADSEN, CARMEN COLON, CASIMIRA MACIAS, SOLEDAD FREGOSO, MANUEL COLON, HILDA VALDES, CARMEN REGALADO, AMERICA SUAREZ, FERDINAND KANGISER, MARIA ROMERO RAFAEL MENDOZA, JOSE LUIZ CORONA, HERIBERTO PIZZARO, RAMON GONZALAS, AND GUILLERMINA OLIVARES,
For Themselves and all Participants in the Reliable Profit Sharing Plan Trust except CHARLES W. LEIGH AND ERVIN F. DUSEK, the Plaintiffs.

Petitioners

v.

CLYDE WILLIAM ENGLE, NATHAN DARDICK, RONALD ZUCKERMAN, LIBCO CORPORATION, TELCO MARKETING SERVICES, INC., TELVEST, INC., THE RELIABLE EMPLOYEES' PROFIT SHARING PLAN TRUST, AND NATIONAL BOULEVARD BANK OF CHICAGO, A National Banking Association.

Respondents

SEPARATE APPENDIX TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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Chicago, Illinois 60603
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Counsel of Record

December 20, 1988

American Reprographics Management, Inc.™ (312) 332-ARMI (800-999-6239)

In the
United States Court of Appeals
For the Seventh Circuit

Nos. 87-2548, 87-2609 and 87-2622

CHARLES W. LEIGH & ERVIN F. DUSEK,

Plaintiffs-Appellants,

and

ESTATE OF GEORGE JOHNSON, et al.,

Intervening Plaintiffs-Appellants, Cross-Appellees,

v.

CLYDE WILLIAM ENGLE, et al.,

Defendants-Appellees, Cross-Appellants.

Appeals from the United States District Court
for the Northern District of Illinois, Eastern Division.
No. 78 C 3799—**Brian Barnett Duff**, *Judge.*

ARGUED APRIL 8, 1988—DECIDED SEPTEMBER 21, 1988

Before BAUER, *Chief Judge*, CUMMINGS and CUDAHY, *Circuit Judges*

CUDAHY, *Circuit Judge.* We revisit a plethora of issues left open in our decision in *Leigh v. Engle*, 727 F.2d 113 (7th Cir. 1984) ("*Leigh I*"). The district court's thorough opinion makes our task less arduous. *See Leigh v. Engle*,

669 F. Supp. 1390 (N.D. Ill. 1987) ("*Leigh II*"). We conclude that the trial judge ably applied *Leigh I* on remand; therefore we affirm.

I.

The facts are fully discussed in *Leigh I*, 727 F.2d at 115-21. We will sketch out only those necessary to this appeal.

Plaintiffs are beneficiaries of the Reliable Manufacturing Corporation Employees Profit Sharing Trust ("Reliable Trust").[1] They contend that defendants violated fiduciary duties under ERISA, by investing trust assets in corporate control contests with which defendants were associated.

The defendants are a network of individuals and companies associated with defendant Clyde Engle, a financier and investor. In particular, Libco is a company controlled by Engle. The administrators of the Reliable Trust, Nathan Dardick and Ronald Zuckerman, were officers or directors of several Engle-controlled entities. We will refer to the complete Engle network, fully described in *Leigh I*, 727 F.2d at 116-18, as the "Engle group."[2]

The suit concerns the trust's investments in three common stocks of interest to the Engle group. For the details of these transactions, *see id.* at 118-21. The Engle Group and the Reliable Trust bought into Berkeley Bio Medical, Inc. ("Berkeley"), at the request of that company's management to help defend against a takeover attempt by Cooper Laboratories, Inc. ("Cooper"). Cooper eventually

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[1] The original plaintiffs, Charles W. Leigh and Ervin F. Dusek, are not parties to this appeal. We will refer to intervening plaintiffs as "plaintiffs" for purposes of this opinion.

[2] The present trustee, National Boulevard Bank, became trustee after most of the events at issue here, and is not part of the Engle group. The only allegation against the bank is undue delay in distributing assets. *See infra* pp. 8-10.

bought the Engle group's shares, giving the group a large profit. In the case of Outdoor Sports Industries, Inc. ("OSI"), the Engle group was the raider. Eventually, a "white knight" came to OSI's rescue, and the Engle group and the trust sold their shares, garnering a profit in excess of one hundred percent in approximately a one-year period. The group and Reliable Trust also bought stock in Hickory Furniture Company ("Hickory"). Engle gained control of the company, and the trust sold its shares after a year at a four percent profit.

The Reliable Trust's return on these three investments was a whopping 72 percent over a relatively brief time span. Nonetheless, plaintiffs brought this action, claiming the administrators breached their duty of loyalty to the trust under the Employee Retirement Income Security Act of 1974, 29 U.S.C. §§ 1001-1461 ("ERISA"), and seeking the Engle group's entire profits from its investments in the three stocks, estimated at up to ten million dollars.

The trial court initially found for the defendants. We reversed in *Leigh I*, holding that the administrators had breached their fiduciary duties under ERISA sections 404 and 406, 29 U.S.C. §§ 1104, 1106, and that plaintiffs might be entitled to some damages, albeit not the amount they requested. We remanded the case for a determination whether Engle and Libco were liable as fiduciaries with respect to the investments; whether the administrators and the bank unduly delayed distribution of trust assets; whether plaintiffs suffered any damages; and for a determination of fees. *Id.* at 140-41.

The district court held that Engle and Libco breached their fiduciary duties by failing to adequately supervise the administrators selected by them. The court found no undue delay in asset distribution. It awarded plaintiffs $6,704 in damages, the difference between the return on Hickory stock and that from a prudent alternative investment. Finally, the court allowed plaintiffs fees incurred

through the time of *Leigh I*, and allowed some defendants partial fee reimbursement from the trust.[3] Both sides appeal.

In a probably futile attempt to clarify the analysis, we will divide our discussion into three categories. Initially, we will review the district court's findings on liability to determine whether they are factually or legally erroneous. Then we will examine the court's calculation of damages. Finally, we will look at the fees questions.

II.

The district court made two findings on liability; the losing parties appeal. We will reverse factual findings only if they are clearly erroneous. *See* Fed. R. Civ. P. 52(a); *Anderson v. City of Bessemer City*, 470 U.S. 564, 573 (1985). "Where there are two permissible views of the evidence, the factfinder's choice between them cannot be clearly erroneous." *Anderson*, 470 U.S. at 574. We review legal determinations de novo.

A.

In *Leigh I*, we ordered the district court to determine whether Engle and Libco acted reasonably and prudently in light of their knowledge of the administrators' conflicting interests and the trust's investments. 727 F.2d at 136. We held that Engle and Libco were fiduciaries of the trust with respect to selection and retention of the Plan's administrators, *id.* at 134, and stated that they had a duty "to take prudent and reasonable action to determine whether the administrators were fulfilling their fiduciary obligations." *Id.* at 135.

Judge Duff held on remand that "Engle and Libco did not take reasonable action to ensure that Dardick and

[3] The dollar amounts have yet to be determined. That fact does not affect the finality of the judgment. *See, e.g., Barrington Press, Inc. v. Morey*, 816 F.2d 341, 342 (7th Cir.), *cert. denied*, 108 S. Ct. 249 (1987).

Zuckerman were fulfilling their fiduciary duties." *Leigh II*, 669 F. Supp. at 1395. His key factual finding was that Engle and Libco "knew of, but chose to ignore" the administrators' improper investment decisions. *Id.* That finding, in conjunction with our opinion in *Leigh I*, made the ultimate finding of liability "almost inevitable." *Id.* at 1417.

Engle and Libco appeal. They do not attack the finding that they knew of the investments. Instead, they contend that even assuming total knowledge of the administrators' actions, they were under no duty to respond. This attack takes two approaches. The first is a thinly-veiled assault on *Leigh I*'s central holding. Engle and Libco argue that the investments were not speculative and that "[t]here was no actual conflict of interest." Reply Brief of Engle and Libco at 5. The latter assertion directly contradicts our holding in *Leigh I* that the administrators breached their duty of loyalty to the trust. 727 F.2d at 132. We will not reopen that can of worms. Also, whether the investments were speculative is irrelevant. The administrators' breach did not consist of investment in speculative assets. Rather, the administrators breached their duties when they made investment decisions out of personal motivations, without making adequate provision that the trust's best interests would be served.[4] That breach, known to Engle and Libco, created a duty on their part to take action to rectify the situation. They did not do so, thereby breaching their supervisory duties.

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[4] *See Leigh I*, 727 F.2d at 132, where we concluded that the administrators had breached their fiduciary duties

> because the fiduciaries had divided loyalties with clear potential for conflicts of interests, because the fiduciaries with divided loyalties failed even to seek independent, disinterested advice regarding these investments and their duties to the plan beneficiaries and because, throughout prolonged contests for corporate control, the fiduciaries' use of the trust assets dovetailed at all times with the interests of the Engle group.

Engle and Libco's more substantial argument is that *Leigh I* should not apply retroactively. They say that *Leigh I* created a new basis for liability from whole cloth, and that it would be "punitive" to hold them liable when they could not have recognized that the administrators were violating the statute. They point us to *City of Los Angeles Dept. of Water and Power v. Manhart*, 435 U.S. 702 (1978), where the Court refused to award retroactive relief in a Title VII action brought against plan adminstrators.

Manhart is inapposite. First of all, it is a Title VII case, construing that statute's unique retroactive relief provisions. *Id.* at 718. Second, the *Manhart* Court's reasoning cuts against Engle and Libco. The *Manhart* Court was concerned that "major unforeseen contingencies" could wreak havoc on the nation's pension plans, destroying the entire system. *Id.* at 721. No such concerns are present here. *Leigh I* did not announce any fundamental change in the rules governing ERISA plan administration. At bottom, the case simply held that administrators violate their duty of loyalty when they use plan assets to dabble in their business associates' takeover attempts, unless there have been special efforts to identify and preserve the trust's best interests. *Leigh I*, 727 F.2d at 132. We fail to see anything novel or unpredictable in this holding. While ERISA is a fairly modern creature, the law of fiduciaries, codified in the Act, is of venerable vintage. *Leigh I* was an application of principles at the heart of corporate and trust law, principles that should be common knowledge to every fiduciary. *Cf. Fulton Nat'l Bank v. Tate*, 363 F.2d 562, 570-71 (5th Cir. 1966); Restatement (Second) of Trusts § 170 (1959) ("the trustee is under a duty . . . to administer the trust solely in the interest of the beneficiary").

Engle and Libco briefly raise other points, all assaulting the notion that they could *ever* he held liable for this sort of conduct. Those arguments must fail in light of *Leigh I*.

B.

The district court's second finding on liability was that "the defendants did not breach their fiduciary duties by delaying the distribution of trust assets." *Leigh II*, 669 F. Supp. at 1412. Plaintiffs appeal this determination.

Judge Duff's holding on this point consists of two parts. He first found that "there was neither a complete discontinuance of contributions nor a complete termination of the plan prior to February 28, 1979." *Id.* Appellants concede this point. Opening Brief of Intervening Plaintiffs-Appellants at 42. They thus must dispute the court's second finding that, given the 1979 termination date, initial distributions were not due until March 1, 1980. *Id.*

Plaintiffs' first argument is that Judge Duff ignored this court's mandate in *Leigh I*. In that opinion, we remanded so that the district court could reconsider the delay issue. 727 F.2d at 136-37. The district court's exhaustive factual findings and its common-sense construction of the relevant documents and regulations compel affirmance. The reasons for any delay become relevant only when distribution is delayed beyond the time mandated by the trust instruments.

Appellants act as though this approach is somehow dishonest. We are hardly inclined to discipline a trial judge for finding the crux of an issue and beginning at that point. Contrary to appellants' overzealous assertions, we did not require the district court to find liability or to follow any one theory in determining liability. In fact, the mode of analysis adopted by the district court was suggested in our opinion, when we urged the court to consider the trust documents and relevant regulations to determine at what point distribution was required. *See id.* at 136.

As to the factual finding that distributions were not due prior to March 1, 1980, we are persuaded by Judge Duff's reasoning. Section 7.2 of the Restated Plan says that "[u]pon termination of the Trust, the Committee shall direct the Trustee to distribute all assets remaining in

the Trust. . . ." Intervening Plaintiffs say that use of the word "upon" requires *immediate* distribution.

The district court properly rejected that rigid interpretation, for several reasons. Nothing in section 7.2 purports to establish the time or manner of distribution. Use of the word "upon" provides little or no guidance. Therefore, Judge Duff properly looked elsewhere for interpretive assistance. As directed by *Leigh I*, 727 F.2d at 136, he looked to the governing law, 26 U.S.C. § 401(a)(14), which, although not applying directly to this type of termination, gives some guidance. That section requires that payments begin no later than sixty days after the close of the termination year. Likewise, in construing the word "upon" in other sections of the Restated Plan, section 5.6 adopts the same rule. We believe Judge Duff correctly looked to closely analogous termination provisions to determine when payments must begin under section 7.2.

Appellants contend that "upon" means something different in section 7.2 than elsewhere in the Restated Plan. But there is not a scintilla of evidence, either in the trust documents or elsewhere in the record, to support that assertion. We will not reject the district court's analysis in favor of mere speculation.

Likewise, the court's alternative holding independently supports its result. Judge Duff held that "[e]ven if defendants had delayed distribution of trust assets, the damages assessed in . . . this court's decision would compensate plaintiffs for any loss they suffered by reason of the delay." District Court Opinion at 46. That finding is clearly correct. The only possible loss from delay is the opportunity cost of not being able to invest the money elsewhere. The trust assets greatly appreciated in value during the period of the alleged delay. Appellants do not challenge this fact, which is dispositive on the damages question. We affirm the district court's finding on this point.

III.

The parties raise two questions as to the district court's calculation of damages. The court rejected plaintiffs' contention that they were entitled to *all* profits on all Engle group investments in OSI, Berkeley and Hickory, holding that defendants showed that their profits were not obtained through use of the trust assets. Judge Duff did, however, award plaintiffs $6,704 in damages from the trust's investment in Hickory, since that stock did not perform as well as more appropriate investment vehicles. We are not surprised that both sides appeal. In *Leigh I*, we called this damage calculation a "formidable task." The district court did an admirable job with it.

A.

Plaintiffs ask for millions of dollars in damages, claiming that all or most of the Engle group's profits from its investments in the three companies were attributable to use of trust assets. We thought we had laid this argument to rest in *Leigh I*, where we examined the facts and the relevant statutes and said that "[t]he plaintiffs' argument reaches too far." 727 F.2d at 137.

Our holding in *Leigh I* was that 29 U.S.C. section 1109 only allows recovery "where there is a causal connection between the use of the plan's assets and the profits made by fiduciaries on the investment of their own assets." 727 F.2d at 137. We also held that "the trustee has the burden of showing which property and profits are his." *Id.* at 138. We tried to make clear to the plaintiffs how unlikely they were to obtain substantial damages, given the investments' excellent returns and the miniscule percentage of the Engle group's total investment made up of trust assets. *See id.* at 137 n.35 (trust never held even one percent of target companies' stock). Appellants characterize the Engle group's profits as a "windfall," Opening Brief of Appellants at 5, but, if that windfall resulted from defendants' own efforts, it in no way belongs to the trust. *See Leigh I*, 727 F.2d at 138. Plaintiffs once again ac-

cuse Judge Duff of ignoring this court's mandate (an accusation they make far too often and with no apparent thought as to whether it is appropriate, *see* Opening Brief of Appellants at 22 n.5), but that "mandate" included a caveat that the judge on remand might very well find *no* damages appropriate. *Leigh I*, 727 F.2d at 138. In order to avoid disgorgement of part of its profits, the Engle group had to show that they did not result from misuse of trust assets. Judge Duff correctly held that defendants met this burden.

There are at least five theories that might explain how use of trust assets increased the Engle group's profits on its own investments. First, perhaps the Engle group effectively "parked" stock by buying it with trust assets. That is, the group might have delayed disclosure of its investment in a target, allowing it to purchase more shares at a lower, pre-disclosure, price, by not including the trust's shares in determining when the group's investments met the threshold for disclosure mandated by federal securities laws. *See* Securities Exchange Act § 13(d), 15 U.S.C. § 78m(d). That contention will not fly here, since the Engle group included the trust's holdings in its Schedule 13D filings. Likewise, any assertion that the Engle group would not have been able to purchase the stock with its own money lacks support in the record. Engle's reputation as an effective financier was based in part on his ability to quickly raise capital.

Third, the increase in the Engle group's holdings due to the trust's investments might have convinced the management of OSI to seek a "white knight," motivated Berkeley's buyer to pay a premium for the Engle group's shares or allowed the group to gain control of Hickory. Judge Duff found these contentions implausible. Those findings are not clearly erroneous. The trust's holdings were a tiny fraction of the Engle group's holdings. The Engle group's efforts succeeded because of its large stake, its ability to raise capital for a larger investment and Engle's reputation as an effective takeover artist. If anything, the trust benefited from its association with Engle, not vice versa.

Fourth, the administrators did not, in the case of Berkeley, have the potential to undermine a settlement between the Engle group and Cooper by refusing to tender the trust's shares. Cooper Laboratories would not have refused to purchase the Engle group's large stake but for the inclusion of the few shares held by the Reliable Trust. There is substantial evidence in the record to support Judge Duff's finding on this point, most notably the testimony of expert witness Daniel Fischel. Plaintiffs offered no persuasive evidence to the contrary, referring primarily to an affidavit of Joseph Dornig, a Cooper officer, never accepted into evidence. Plaintiffs rely on a single inconclusive statement taken out of context. They make no detailed argument as to why the affidavit should have been admitted. Even if it had been, the result would not have changed.

Finally, Judge Duff's finding that trust purchases did not substantially affect the market price of stock is not clearly erroneous. Plaintiffs' arguments on this point consist mostly of attempts to denigrate the testimony of Daniel Fischel, an expert called by the defendants. We have reviewed Professor Fischel's testimony and agree with Judge Duff's characterization of it as "highly credible and persuasive." *Leigh II*, 669 F. Supp. at 1401. Professor Fischel exhaustively analyzed the economic facts of the case. Essentially the district court believed Fischel and disbelieved plaintiff's experts. We cannot call findings based on such thorough analysis clearly erroneous.

B.

Once the district court determined that the Engle group's profits were not tainted by the trust's investments, it had to determine whether the Trust suffered *any* losses attributable to the distorted investment decisions that may have resulted from the trustees' conflicts of interest. Judge Duff undertook the straightforward approach of comparing the return on the improper investments with that of a reasonably prudent alternative investment—in this instance the Harris Bank's common

stock funds. In *Leigh I* we placed the burden of disproving damages on the defendants. 727 F.2d at 138. Therefore, the court adopted the "most generous" of the reasonable damage calculations submitted to it. *Leigh II*, 669 F. Supp. at 1405. Looking at each of the three trust investments in isolation, it found that the trust suffered no losses from the OSI and Berkeley investments. It did, however, find a loss of $6,704 on the Hickory investment. While that investment made a small profit, the gain was less than that from the alternative investment used as a standard by the court.

Defendants appeal this award. They contend, not without foundation, that the court erred in not looking at the value of the entire portfolio in determining whether the trust suffered any loss from the investments. Once again a party alleges that Judge Duff misconstrued or ignored this court's mandate; once again we do not agree. We did say in *Leigh I* that "[i]t is clear that the trust lost no money in the challenged transactions." 727 F.2d at 121-22. Judge Duff did not find differently. He merely found that the *gain* from the Hickory investment was less than that which would have been obtained through prudent alternative investments.

Turning to the theoretical challenge, we find that defendants' arguments contain a kernel of truth. When investment advisors make decisions, they do not view individual investments in isolation. Rather, the goal is to create a diversified portfolio that balances appropriate levels of risk and return for the investor. The risk of a given investment is neutralized somewhat when the investment is combined with others in a diversified portfolio. The risk inherent in the entire portfolio is less than that of certain assets within that portfolio. Ideally, after diversification only market risk remains. Likewise, the return from a portfolio over time should be more stable than that of isolated investments within that portfolio. (This discussion is greatly simplified; for a somewhat more technical explanation, *see* R. Brealey & S. Myers, *Principles of Corporate Finance* 119-32 (2d ed. 1984).)

Given the facts that investment advisors generally follow a portfolio strategy of investment and that beneficiaries whose assets are being managed are concerned with the end result of that strategy, not with the return on a single element in the portfolio, it makes sense for courts to look at the whole portfolio to determine the investment strategy's success. *Cf. Donovan v. Bierwirth*, 754 F.2d 1049, 1057 (2d Cir. 1985); Landes & Posner, *The Revolution in Trust Investment Law*, 63 A.B.A.J. 887, 889-90 (1976); Note, *Fiduciary Standards and the Prudent Man Rule Under the Employment Retirement Income Security Act of 1974*, 88 Harv. L. Rev. 960, 967 (1975).

Judge Duff acknowledged this theory's force as a general principle, but determined that it should not apply in this case. Although the question is a close one, we do not believe he abused his discretion. Portfolio theory gains its force from the fact that it reflects investment decisions in the real world. But that assumption does not hold in this case. As we held in *Leigh I*, defendants did not make their investment decisions with the sole goal of creating a diversified, safe portfolio for the trust beneficiaries. They argue that their decisions had that *effect* and that the trust made a great deal of money; but the result does not change the fact that the trustees' purposes were not those of portfolio investors. The administrators looked at the stocks in isolation; so a court is justified in taking the same view when calculating the loss from those investments. Our holding may be reduced to this: where fiduciaries breach their duty of loyalty by making individual investments with an eye toward some goal other than the creation of a proper portfolio for their clients, a court may return the favor, viewing the investments in isolation to determine damages.

One might argue that this rule results in overdeterrence, that trustees will be deterred from making potentially profitable and prudent investment decisions by the risk of future damages. That might be the case if the rule were applied to marginal conduct, e.g., to an investment strategy that borders on an unacceptable risk level but

is close to the range of reasonableness. That is not this case. Here the trustees did not err slightly in their attempt to create a proper portfolio; they simply made no such attempt, at least with respect to the decisions to purchase stock in OSI, Berkeley and Hickory. There is no way to overdeter such conduct. It should *never* occur, no matter how profitable the end result.

In short, the appeal and cross-appeal on damages lack merit. Plaintiffs ask for the moon, a possibility we firmly rejected in *Leigh I*. Defendants, on the other hand, seek to avoid even a modest penalty for their misconduct. The district court struck a defensible middle approach, one much more in tune with the case's realities than the arguments of any party. *Cf. Patton v. Mid-Continent Sys., Inc.*, 841 F.2d 742, 748 (7th Cir. 1988).

IV.

Finally, we must visit the issue of fees. Judge Duff held first that the trust instruments allowed for reimbursement of fees incurred by Dardick, Zuckerman and National Boulevard Bank, for defense of claims on which plaintiffs did not prevail. For their efforts in prosecuting the sole issue on which they did prevail he awarded plaintiffs fees. Because determination of exact fees incurred in litigating specific issues is well-nigh impossible in this case, and because the parties have evidenced an uncanny proclivity for making every molehill into a mountain, he made the solomonic decision to award plaintiffs all fees incurred through *Leigh I*, but none thereafter. Extended fee litigation would serve no purpose except to further deplete the trust, and the issues on which plaintiffs prevailed were substantially resolved by our first decision. Moreover, "[a]warding attorneys' fee to plaintiffs for this most recent portion of the case would reward litigation that was ill-conceived, often poorly executed, and fractious." *Leigh II*, 669 F. Supp. at 1417. Both sides appeal.

A.

Plaintiffs ask us to reverse the decision allowing reimbursement of fees to Dardick, Zuckerman and National Boulevard Bank, incurred in fighting claims that ultimately failed. We cannot say that the trial court abused its discretion.

The trust instruments allow for reimbursement of fees, and allow a reserve to be set up to ensure payment. The only real question is whether the trust provisions conflict with ERISA. They do not. While an award of fees to a losing defendant certainly would contravene Congress' intent, *see* 29 U.S.C. § 1110(a), plaintiffs point us to no statutory or common-law basis for denying fees to a *prevailing* trustee where the trust documents specifically contemplate such reimbursement.

Plaintiffs argue that this result unjustly deprives the beneficiaries of their funds. We sympathize, to the extent that plaintiffs think it is disgraceful for pensioners to be deprived of their benefits because of this seemingly endless litigation. To the extent they try to place the blame for this result entirely on the defendants, however, plaintiffs are mistaken. Defendants *prevailed* as to most of the claims. The record makes painfully clear that plaintiffs (or their attorneys) needlessly prolonged this litigation through quixotic, short-sighted and hardball tactics that were apparently undertaken with little thought as to the effect on the ultimate victims—the beneficiaries. Defendants expended great sums of money defending meritless claims. Very few people would become plan administrators if subjected to such unjust, extensive potential costs. Reimbursement here conformed with the trust documents and ERISA. We therefore affirm that aspect of the district court's holding.

B.

Judge Duff awarded plaintiffs fees incurred through *Leigh I*. We give great deference to this determination, committed by statute to the trial court's discretion. 29

U.S.C. § 1132(g)(1). Both sides appeal. Plaintiffs want more money; defendants say plaintiffs should get nothing. In *Leigh I* we set out the legal standard to be applied on remand. *See Leigh I*, 727 F.2d at 139 n.39. The court below followed that analysis, considering five factors:

> (1) The degree of the opposing parties' culpability or bad faith; (2) the ability of the opposing parties to satisfy an award of fees; (3) whether an award of fees against the opposing parties would deter others from acting under similar circumstances; (4) whether the parties requesting fees sought to benefit all participants and beneficiaries of an ERISA plan or to resolve a significant legal question regarding ERISA; and (5) the relative merits of the parties' positions.

Id. (quoting *Marquardt v. North Am. Car Corp.*, 652 F.2d 715, 717 (7th Cir. 1981)). The district court found:

> (1) Dardick, Zuckerman, Libco, and Engle were grossly negligent in investing a substantial portion of the trust's assets in three speculative stocks. (2) The four breaching fiduciaries have the resources to pay a fee award and are better able than plaintiffs to bear this cost. (3) An award of attorneys' fees to prevailing plaintiffs will tend to deter similar fiduciary misconduct in the future. (4) Plaintiffs (or at least intervening plaintiffs) brought this lawsuit on behalf of all plan participants, not merely for individual gain. (5) The liability of the four breaching fiduciaries is not a close question; even minimal reflection should have led them to realize it was unlawful to invest 30 percent of the trust's assets in three speculative stocks.

Leigh II, 669 F. Supp. at 1416.

Defendants challenge this characterization of the case, but we cannot say it is so wild as to be an abuse of discretion. In particular, the deterrent effect of a fee award looms large on these facts. As matters turned out, the trust suffered little damage. But that does not make defendants' misconduct less censurable. Defendants' briefs in this court exhibit a disturbing inclination to downplay

the gravity of their offense because it made money. We agree with the court below: "Perhaps the defendants are too young, too wealthy, and too comfortable to have contemplated the enormity of the risk they took, and the human suffering so narrowly averted." *Id.* at 1417. A fee award is one small way to impress upon them the gravity of their conduct, and to deter such action in the future.

Plaintiffs challenge the amount of the award. Again, the abuse of discretion standard applies. *Bright v. Land O'Lakes, Inc.*, 844 F.2d 436, 442 (7th Cir. 1988). In this context, "an abuse of discretion occurs only when no reasonable person could take the view adopted by the trial court. If reasonable persons could differ, no abuse of discretion can be found." *Harrington v. De Vito*, 656 F.2d 264, 269 (7th Cir. 1981), *cert. denied*, 455 U.S. 993 (1982).

The court below allowed plaintiffs' fees incurred prior to *Leigh I*. Although the judge found that they prevailed only as to one issue, he felt that attempting to coerce these parties into dividing fee requests by issue would be costly, time-consuming and probably not fruitful.

The district court's approach is far from unreasonable. Judge Duff correctly asserts that *Leigh I* "established the only significant legal principles to arise from this lawsuit, and also resolved the principal factual issues on which plaintiffs prevailed." *Leigh II*, 669 F. Supp. at 1416. Our first opinion made clear that while plaintiffs proved a breach of duty, they were probably not greatly injured by that breach. To continue in hope of a jackpot was mere folly, and it should not be rewarded. The district court's approach ensures that the trust will not be further depleted by years of fee litigation. We affirm.[5]

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[5] Plaintiffs also request sanctions in their reply brief under Fed. R. Civ. P. 11, Circuit Rule 38 and 28 U.S.C. section 1927. Rule 11 sanctions are of course not available from this court on appeal. *Hays v. Sony Corp.*, 847 F.2d 412, 420 (7th Cir. 1988). Moreover, to the extent anyone should be sanctioned for abusing the litigation process, it is not the defendants. Plaintiffs sometimes tread

(Footnote continued on following page)

V.

Judge Duff best characterized this case.

> Perhaps only Charles Dickens could savor this litigation. For nearly a decade now, the parties have fought bitterly over the Reliable trust, the only noticeable effect being the steady diminution of its assets. The advocacy has been harsh and often vituperative: lawyers have accused each other of personal wrongdoing, discovery disputes continued through the last day of trial, and shouting matches have broken out. If it were possible to bottle the contempt, even hatred, which the lawyers and parties feel for one another, there would be enough to sustain a small civil war for months. The great length and extraordinary difficulty of this litigation owes much to the depth of the combatants' animosity.

Leigh II, 669 F. Supp. at 1417. This is a case that existed, through much of its ten-year life, almost solely for the benefit of the lawyers. That is indeed unfortunate, for the costs are borne most heavily by those whom ERISA was intended to protect—beneficiaries and their families. We wish the trustees had considered the consequences of their actions before breaching their duty of loyalty to the beneficiaries. We also wish, however, that plaintiffs' counsel had paused for a moment to realistically assess, at each stage of the game, the impact of extensive litigation on their clients. Had they done so, everyone involved would have been better off.

AFFIRMED.

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[5] *continued*
perilously close to personal insults against opposing parties and against the trial judge, whom we feel did an admirable job. *Cf. United States v. Byrski*, No. 88-1725, slip op. at 10-11 (Aug. 5, 1988). We have noted before the unfortunate tendency of parties to request sanctions far too often and with little or no reasoned argument. *See Meeks v. Jewel Cos.*, 845 F.2d 1421, 1422 (7th Cir. 1988). This case is a prime example of the species.

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United States Court of Appeals

For the Seventh Circuit
Chicago, Illinois 60604

September 30, 1988.

Before

Hon. WILLIAM J. BAUER, Chief Judge
Hon. WALTER J. CUMMINGS, Circuit Judge
Hon. RICHARD D. CUDAHY, Circuit Judge

Nos. 872548, 87-2609 and 87-2622

CHARLES W. LEIGH &
ERVIN F. DUSEK,
Plaintiffs-Appellants,
and
ESTATE OF
GEORGE JOHNSON, et al.,
Intervening Plaintiffs-Appellants, Cross-Appellees,
v.
CLYDE WILLIAM ENGLE,
et al.,
Defendants-Appellees, Cross-Appellants.

Appeals from the United States District Court for the Northern District of Illinois, Eastern Division.

No. 78 C 3799

Brian Barnett Duff, Judge.

ORDER

The slip opinion published on September 21, 1988 in the above-entitled matter is hereby amended as follows:

Page 13, line 8, should read "Langbein & Posner" instead of " Landes & Posner. "

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

CHARLES W. LEIGH and
ERVIN F. DUSEK,
Plaintiffs,

ESTATE OF
GEORGE JOHNSON, et al.,
Intervening Plaintiffs,
v.

CLYDE W. ENGLE, et al.,
Defendants.

No. 78 C 3799

FINDINGS OF FACT AND CONCLUSIONS OF LAW

This action under the Employee Retirement Income Security Act ("ERISA"), 29 U.S.C §§ 1001-1461 accuses defendants of misusing the assets of an employees' profit-sharing trust. Defendants allegedly invested a substantial portion of the trust's assets in three speculative stocks for the purpose of enhancing their own investments in those stocks, and delayed distribution of trust assets to beneficiaries in order to profit by prolonging their control of the trust's stock holdings.

Plaintiffs and intervening plaintiffs (collectively, "plaintiffs") are vested beneficiaries of the trust, which is subject to ERISA. There are five defendants: Nathaniel Dardick and Ronald Zuckerman, the trust's two administrators; Libco Corp. ("Libco"), which owned 100 percent of Reliable Manufacturing Co. ("Reliable"), the company that sponsored the trust and had direct authority to appoint and retain its administrators; Clyde Engle, who controlled at least 49 percent of Libco's stock and was chairman of its board of directors; and National Boulevard Bank ("National Boulevard"), the trustee of the Reliable trust.

Defendants prevailed in a 1982 trial before Judge George Leighton. The Seventh Circuit vacated and remanded, *Leigh* v. *Engle,* 727 F.2d 113 (7th Cir. 1984), and in so doing resolved numerous factual and legal issues. Of particular importance to this proceeding are the Seventh Circuit's conclusions that Dardick and Zuckerman breached their fiduciary duties to the trust by investing its assets as they did, 727 F.2d at 132, and that Libco and Engle were fiduciaries of the trust to the extent they were responsible for selecting, retaining, and supervising the trust's administrators, 727 F.2d at 133, 135-36.

The Seventh Circuit's opinion left four issues for resolution in a second trial:

> 1. Did Libco and Engle breach their fiduciary reponsibilities by inadequately supervising Dardick's and Zuckerman's investment activities, in light of Libco's and Engle's knowledge that Dardick and Zuckerman faced conflicting loyalties in investing trust assests?
>
> 2. What, if any, restitution is due the trust from those defendants found to have breached their fiduciary duties with respect to investment of trust's assets?
>
> 3. Did Dardick, Zuckerman, and the National Boulevard Bank breach their fiduciary duties to the trust by delaying distribution of its assets, and did Libco and Engle breach their fiduciary duties by failing to supervise Dardick, Zuckerman, and the National Boulevard Bank in this regard? If so, what restitution is due?
>
> 4. Must defendants restore to the trust money used to pay their attorneys' fees during this litigation, and should the court award attorneys' fees to either party under 29 U.S.C. §§1132(g) (1)?

In addition, plaintiffs have raised a fifth issue which was not before either Judge Leighton or the Seventh Circuit:

> 5. Should the court assess punitive damages against those defendants found to have breached their fiduciary duties?

The parties tried these issues to the court on 14 full trial days from July 21 to August 6, 1986, and the court now makes its findings of fact and conclusions of law. Before proceeding, however, two preliminary comments are in order. First, the Seventh Circuit made detailed findings of fact from the record on appeal. Those findings, which the court repeats only where necessary, form the starting point for this court's decision. Second, the final line of the Seventh Circuit's opinion reads "Vacated And Remanded." The parties disagree about whether this vacates Judge Leighton's findings of fact in their entirety, or vacates only those findings of which the Court of Appeals specifically disapproved. Resort to a dictionary settles the matter. To "vacate" comes from the Latin verb *vacare* for "be empty," and means to annul or leave empty. *Webster's Third New International Dictionary,* 2527 (1981). *Accord, Black's Law Dictionary,* 1388 (5th ed. 1979). Because Judge Leighton's findings of fact have been "left empty," they have no continued vitality except insofar as the Seventh Circuit may have adopted certain findings and made them their own.

I. BREACH OF FIDUCIARY DUTY BY LIBCO AND ENGLE

A. Findings of Fact

1. Reliable's board of directors, which included Engle and George Contarsy, Libco's president, appointed Dardick and Zuckerman administrators of the Reliable Employees Profit-Sharing Trust. Before the Reliable board did so, neither Engle nor Contarsy nor any other member of either Reliable's or Libco's board made any inquiry into Dardick's

or Zuckerman's experience with the administration of profit-sharing trusts, or into their knowledge of ERISA. Engle L-316-17; Contarsy L-427.[1] So far as Engle and Libco knew, Dardick and Zuckerman had no such experience or knowledge. *Id.*

2. Neither Dardick nor Zuckerman received pay for their services as trust administrators, but both received substantial income from other activities related to Engle's business endeavors. 727 F.2d at 117; Zuckerman at L-442-44.

3. At the direction of Dardick, who made all investment decisions for the Reliable trust, 727 F.2d at 117, PX 149 at 27, the trust purchased 15,800 shares of Berkeley Bio Medical, Inc. ("Berkeley") for a total of $71,480 between March 17 and March 21, 1978. PX 427. The trust also purchased 12,500 shares of Outdoor Sports Industries, Inc. ("OSI") at a cost of $77,734 between March 22 and April 11, 1978. *Id.* In addition, the trust purchased 8,000 shares of Hickory Furniture Co. ("Hickory") for $43,000 on March 22, 1978, and 4,000 more shares for $29,433 on June 9, 1978. *Id.* The total cost of the Berkeley, OSI, and Hickory purchases was $221,647, and represented approximately 30 percent of the trust's assets. *Id.*; 727 F.2d at 118. The trust never bought more stock in these companies.

4. Engle and persons and entities with whom he maintained business affiliations (collectively, "the Engle group") made substantial investments in Berkeley, OSI,

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[1] The court uses the following abbreviations in citing to the record: (1) a name followed by page numbers refers to the transcript of testimony at this trial: (2) a name followed by "L", followed by page numbers refers to the transcript of the trial before Judge Leighton; (3) DX and PX refer to defendants' and joint plaintiffs'-intervenors' exhibits; L-DX and L-PX refer to defense and plaintiff-intervenor exhibits originally admitted in the trial before Judge Leighton; P1X and IntX refer to exhibits in this trial offered solely by plaintiffs or intervening plaintiffs.

and Hickory beginning before and continuing after the trust's purchases of stock in those three companies. PX 427, DX 600 at Ex. D-F. The Engle group eventually acquired 10.7 percent of Berkeley, 22 percent of OSI, and a majority of Hickory. 727 F.2d at 119 n. 10. Prior to the start of the trust's purchases, the Engle group owned 95,220 shares of Berkeley, bought for approximately $476,500; 9,000 shares of OSI, bought for $41,359; and 50,400 shares of Hickory, bought for $258,001. PX 427. Because of his roles as Engle's personal counsel and general counsel of Libco, Dardick was aware of most if not all of these holdings by members of the Engle group, 727 F.2d at 117, 130-31, and Engle correspondingly was aware of Dardick's knowledge.

5. Dardick did not invest trust assets in Berkeley, OSI, and Hickory solely for the purpose of creating an investment portfolio to benefit the trust; rather, he did so at least partly to aid the Engle group's stock acquisition program. 727 F.2d at 129-31. While Dardick's motives for investing trust assets as he did are impossible to divine completely, the evidence suggests that a variety of factors besides his desire to aid the Engle group's program may have entered into his decisions: a genuine belief that Berkeley, OSI, and Hickory were good investments, see PX 410; Newbill L-671-75; Zuckerman 477-78, 513; his desire as a young and ambitious lieutenant to emulate Engle's investment strategy; and the ready availability of Newbill's investment advice, which eliminated the need to search out an independent investment counselor, *see* Dardick L-816-17.

6. Engle and Libco knew of the trust's investments no later than April 21, 1978, when Engle disclosed them at a board meeting of Telco Corp. ("Telco"). Engle 842; 727 F.2d at 118. Libco owned 64 per cent of Telco at the time, and Engle was Chairman of the Board of each company. 727 F.2d at 116. Once they learned that the trust had purchased stocks in which the Engle group was

acquiring substantial interests, Engle and Libco knew of a conflict between Dardick's responsibility to invest trust assets solely for the gain of the beneficiaries, and his duty to act in the best interest of his superior.

7. Despite this evident conflict of interest, which persisted until the trust sold its shares of OSI on June 26, 1979 (the trust disposed of its Berkeley and Hickory shares earlier), neither Engle nor any other Libco official ever questioned Dardick's decision to invest a total of 30 percent of the trust's assets in Berkeley, OSI, and Hickory. Engle L-266; Contarsy L432-35. There is no evidence that Engle or any other Libco official ever requested reports from Dardick and Zuckerman on the nature of the trust' investment policy, ever reminded them of their responsibilities as fiduciaries under ERISA, ever asked whether they considered investing in stocks other than the targets of Engle' investment program, ever sought an independent review of their investment decisions, or ever suggested or even contemplated replacing them with independent administrators.

B. Conclusions of Law

1. Engle and Libco were fiduciaries of the trust "with respect to the selection and retention of the plan administrators," 727 F.2d at 134, and "[a]s the fiduciaries responsible for selecting and retaining their close business associates as plan administrators, Engle and Libco had a duty to monitor appropriately the administrators' actions," *id.* at 135. This obliged Engle and Libco "to take prudent and reasonable action to determine whether the administrators were fulfilling their fiduciary obligations." *Id.*

2. Engle and Libco did not take reasonable action to ensure that Dardick and Zuckerman were fulfilling their fiduciary obligations. Engle and Libco knew of, but chose to ignore, Dardick's and Zuckerman's pursuit of a speculative investment policy which risked the trust's assets while

at a minimum creating the appearance of serving Engle's and Libco's own business interests. Accordingly, the court concludes that both Engle and Libco breached their fiduciary duties to the trust.

II. RESTITUTION FOR INVESTMENT OF TRUST ASSETS

A. Findings of Fact

1. When it sold its shares in Berkeley after holding them approximately five months, the trust made a profit of 66 percent on its investment of $71,581. 727 F.2d at 119; DX 600 at Ex. D. The trust sold its shares in OSI after approximately 15 months for a profit of 141 percent on its investment of $77,737. 727 F.2d at 119; DX 600 at Ex. E. The trust sold its Hickory shares after holding them an average of approximately seven months, and made a profit of four percent on its investment of $72,433. 727 F.2d at 119; DX 600 at Ex. F. The trust's aggregate return on these three investments was 72 percent. 727 F.2d at 119.

2. The amount of restitution, if any, due the trust as a result of its investments in Berkeley, OSI, and Hickory has two components: (a) the trust's actual losses from these investments; and (b) the breaching fiduciaries' profits attributable to those investments.[2] DX 600 at 3.

Losses to the Trust

3. The parties dispute whether the court should view the trust's investments in Berkeley, OSI, and Hickory

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[2] Since the breaching fiduciaries' profits are interwoven with those of the Engle group as a whole, the portion of the court's decision addressing the issue of restitution considers the broader and simpler question of whether *any* Engle group member profited from the trust's investments. The court's conclusion that no Engle group member profited from the trust's investments makes it unnecesary to separate the profits of Dardick, Zuckerman, Libco, and Engle from those of the other Engle group members.

individually or as a portfolio for the purpose of determining whether the trust lost money by investing in those stocks. All parties agree that if the court views the trust's stock investments in the aggregate, the trust suffered no loss because its return of 72 percent substantially exceeded what it could have earned through prudent alternative investments. All parties also agree that if the court views each stock separately, the trust suffered no losses on its investments in Berkeley and OSI, but did suffer a loss on its investment in Hickory because other prudent investments would have produced a return in excess of four percent.

4. Defendants' expert witness, Daniel Fischel,[3] testified that the court should consider the three stocks together because they constitute a portfolio. Fischel 652-53; DX 600 at 6. According to Fischel, the trust's beneficiaries care only about the total return on their investment, not about the return on each component stock, or about whether the portfolio is diversified. *Id.* Fischel's testimony on this issue is consistent with that of another expert witness for defendants, Gil Matthews, an investment banker who is a managing director of Bear, Stearns & Co. Like Fischel, Matthews testified that it is appropriate to consider the three stocks together for the purposes of calculating the amount of restitution due the trust. Matthews 2005-06. Investors will always prefer a portfolio which returns an aggregate of 72 percent but includes one stock returning only four percent, to a fully diversified portfolio in which every stock returns 14 percent, Fischel and Matthews suggest.

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[3] Fischel is a professor of law and director of the Law and Economics Program at the University of Chicago Law School. He has published extensively on corporate finance and the securities markets.

5. Plaintiffs' expert witnesses, Joel Stern and Laurence Siegel,[4] testified that the court should consider the returns on the trust's investments in Berkeley, OSI, and Hickory individually because a portfolio consisting only of stocks in three small companies is so undiversified that the stocks simply represent individual purchases. Siegel 1470-72; PX 412 at 11.

6. Lee Meyer, a former trust administrator at Harris Trust and Savings Bank ("Harris") in Chicago, testified that although Harris manages, among others, a fund comprised primarily of highly-speculative stocks issued by small companies, the bank refuses to allow profit-sharing trusts or pension plans to invest more than five percent of their assets in this fund. Meyer L561. Charles Brickman, an investment banker with Kidder Peabody & Co. for 23 years, testified that OSI stock was not an appropriate investment for a profit-sharing trust because OSI's small size and erratic earnings history rendered the stock speculative. Brickman L-517-20. No witness testified that a portfolio consisting solely of stock in Berkeley, OSI, and Hickory would have been diversified. The court finds that the trust's investments in Berkeley, OSI, and Hickory were undiversified and highly speculative.

8. Fischel testified that if the court decides to view the Hickory investment individually, it should assess damages to the trust from that investment by calculating the additional profit the trust would have earned had it made any of three prudent alternative investments.

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[4] Stern is managing partner of Stern Stewart & Co., a New York firm that provides financial advice to industrial companies, banks, and large accounting firms. He is an adjunct professor at Columbia University's Graduate School of Business, has previously served as president of Chase Financial Policy, a division of the Chase Manhattan Bank, and is a rotating panelist on the Wall Street Week television program. Siegel is a selfemployed financial consultant.

According to Fischel, instead of investing a total of $72,433 in Hickory stock in March and June, 1978, and selling it for a four percent profit in March, 1979, the trust could have invested the same amount: (a) in Harris Bank's Investment Reserve Fund (in which the trust's nonstock assets were invested), for an additional profit of $2,109; (b) in Harris Bank's Common Stock Fund, for an additional profit of $3,747; or (c) divided equally among all of Harris Bank's common stock funds, for an additional profit of $6,704. DX 600 at Ex. B.

9. Gil Matthews testified that he measured the performance of the trust's Hickory investments against three alternative financial standards for the purpose of assessing the trust's losses from those investments: (a) long-term debt securities, which indicate no loss by the trust since Hickory stock outperformed the market for long-term debt securities while the trust owned the stock; (b) 12-month Treasury bills, which indicate a loss by the trust of $800; and (c) a general stock market index, which indicates a loss of approximately $2000. Matthews at 2010-12.

10. Stern stated that a fair return on stocks as risky as Berkeley, OSI, and Hickory would have been between 20 and 30 percent annually. Stern 1001; PX 412 at 11. If the trust had earned a 30 percent annual return on its Hickory investment its profits would have been $15,983 greater than they actually were. DX 600 at Ex. B. Neither Stern's testimony nor any other evidence suggests how the trust could have achieved such a high rate of return through any prudent investment.

Gains to the Engle Group
Berkeley

11. Plaintiffs suggest a series of ways in which the Engle group might have profited from the trust's investments in Berkeley, OSI, and Hickory. With respect to Berkeley, they contend that the trust's purchases benefited the Engle group because (a) the trust bought its Berkeley

stock when the Engle group needed to acquire control of additional shares but lacked the cash to do so; (b) the trust's purchases affected Berkeley's stock price; (c) Cooper Laboratories, Inc. ("Cooper") would not have purchased the Engle group's Berkeley stock at a premium unless the trust had agreed to sell its stock to Cooper. Plaintiffs also assert that the Engle group recycled profits from the trust's Berkeley purchases into new and remunerative investments in OSI and Hickory. PX 412 at 7-8. None of these theories has merit.

12. Plaintiffs' first argument is that the Engle group turned to the trust as a means of gaining control over additional shares of Berkeley because in the spring of 1978 no other Engle group member could spare the $71,480 which the trust invested. This argument is plausible only if the Engle group could not wait to gain control of the 15,800 Berkeley shares that the trust purchased; if there was no urgency in the Engle group's acquisition of voting control over those shares, the Engle group would have been better off purchasing the shares in its own name once it accumulated enough money to do so, since profits on those shares then would accrue to the Engle group rather than to the trust.

13. Even assuming it was important for some Engle affiliate to gain control of 15,800 shares of Berkeley stock between March 17 and March 21, 1978 an assumption for which there is not a shred of evidence it is nonsense for plaintiffs to claim that the Engle group was short of cash during this period and therefore turned to the trust as a source of purchasing power. The evidence establishes that the Engle group had ample funds available to buy Berkeley stock in the spring of 1978, had it desired to do so.

14. On of December 31, 1977, Libco had total assets of approximately $48 million. DX 601 at 48. The company had excess funds during 1977 and 1978. Engle 1838. The book value of Telco in 1978 was approximately $11 million,

id. at 1840, and it was able to retain "a substantial part" of monthly income in excess of one million dollars from a leasing portfolio, *id.* at 1838. Another member of the Engle group, GSC Enterprises, Inc., had assets in excess of $109 million as of September, 1978. DX 612. The record lacks detailed financial information about other members of the Engle group, but every indication is that at least two of them – Sierra Capital Group, and Engle himself – had assets that were substantial and separate from Libco's and Telco's assets. *See* IntX 430.

15. On April 17, 1978, Telco announced it had completed a refinancing of certain debts. PX 72 at CR 28-30. Engle informed Telco's board of directors at a meeting on April 21, 1978 that as a result of this refinancing Telco had approximately $2 million in cash available for immediate use. PX 59 at CR 3. On Engle's recommendation the board then authorized Telco's management to purchase up to 200,000 shares of Berkeley at a price not to exceed $6.50 per share; up to 140,000 shares of OSI at a price not to exceed $10.00 per share; and up to 120,000 shares of Hickory at a price not to exceed $5.00 per share. *Id.* at CR 5-6.

16. Fischel testified that many sources of capital were available to the Engle group at the time of the trust's stock purchases, including retained earnings, the capital markets, the partnership market, and personal wealth. Fischel 1754; *accord* Matthews 2032. Even plaintiffs' own expert conceded that $75,000 was a "mere pittance" to a company with assets of $50 million, Stern 638-39, and that members of the Engle group might have been able to come up with capital to acquire an additional $75,000 worth of Berkeley stock in the spring of 1978 if doing so had been important to their investment program, *id.* at 628-29. In the face of this evidence the court finds it inconceivable that the Engle group was so strapped for cash in February, March, and April, 1978 that the only way it could gain control of $71,480 worth of Berkeley stock was through

use of the trust's assets.

17. Plaintiffs' second argument for attributing the Engle group's profits to the trust's investments in Berkeley is that the trust's purchases pushed up the price of Berkeley stock, thereby inflating the value of the Engle group's shares. Oblivious to logic, plaintiffs also make the opposite argument: that the trust's purchases benefitted the Engle group by *preventing* Berkeley's stock price from rising. Both arguments are wrong. The evidence demonstrates that the trust's purchases had at most a negligible effect on Berkeley's stock price.

18. Berkeley's stock price was essentially flat from February 28 to April 17, 1978, a period extending more than two weeks before and three weeks after the trust's purchases. DX 600 at Ex. D.

19. Fischel studied the effect of the trust's purchases on Berkeley's stock price by examining daily changes in the value of Berkeley stock from January 3 to August 31, 1978. He compared the "actual return" from holding a Berkeley share for each market day (taking into consideration changes in the stock price as well as any dividends distributed that day) to the "expected return" from holding a share of stock in a typical company of Berkeley's size and industry for the same day. Fischel 1642-43; DX 600 at 15-16, Ex. D.

20. This analysis, which plaintiffs do not challenge, demonstrates that on the dates of the trust's Berkeley purchases, and on the several days immediately following, there was never any statistically significant difference between the actual return from holding a Berkeley share and the return which would have been expected by someone holding a share of stock in a comparable company. DX 600 at Ex. D, G. Fischel stated that statisticians view a result as statistically significant if the probability of obtaining it by chance is less than five percent, and that he relied on this standard in preparing his analysis. *Id.*

at Ex. G. In simpler terms, Fischel's study establishes the absence of any scientifically reliable link between the trust's purchases and changes in Berkeley's stock price.

21. Fischel's analysis also establishes the absence of any statistically significant price movement on or about the date that Telco's Schedule 13D filing provided the first public disclosure of the trust's purchases. *Id.* at Ex. D.

22. According to Fischel, numerous academic studies have found that stock prices react almost instantaneously to newly available information about a stock. PX 600 at 16. The absence of any statistically significant changes in Berkeley's stock price within several days of the filing of Telco's Schedule 13D therefore suggests that public disclosure of the trust's purchases did not affect the stock price.

23. A look at a graph of Berkeley's day-to-day stock price changes, DX 635, offers a means of gauging the market impact of the trust's purchases and their subsequent public disclosure that is less reliable but more sensitive than Fischel's approach. Fischel's analysis detects only stock price variations so large they almost certainly are not random, while a graph can reveal relationships which, though not statistically significant, are nonetheless real. The graph shows that Berkeley's stock price was almost flat from early February through early June, 1978. In fact, the stock price was *most* stable during the two-week period when the trust purchased its shares. *Id.* The stock price did increase slightly (from $4.625 to $5.000) in the five trading days after Telco filed its Schedule 13D, but it is impossible to attribute this increase to disclosure of the trust's purchases, since Telco bought a total of 35,200 shares during the same five-day period, *id.*, and those purchases would have tended to drive the stock price up if they had any effect at all, *id.* at 9.

24. Even if plaintiffs were correct that the trust's purchases of Berkeley shares drove the company's stock

price up, such an increase would not have benefitted the Engle group. Of the total number of shares it accumulated before selling them, the Engle group acquired substantially more than half after the trust completed its purchases and Telco filed its Schedule 13D. PX 427, DX 600 at Ex. D. Any increase in the price of Berkeley stock attributable to the trust's purchases thus would have harmed the Engle group by forcing it to pay more for the shares it subsequently acquired. Fischel 1701.

25. The court rejects plaintiffs' alternative theory that the trust's purchases aided the Engle group by prolonging the secrecy of its acquisition program, thereby enabling members of the group to accumulate additional shares before disclosure of the program triggered a price increase. Even assuming that disclosure of the Engle group's activities did cause Berkeley's stock price to rise – a dubious assumption since the evidence shows there was no meaningful market reaction to Telco's Schedule 13D filing – Telco included the trust's Berkeley shares in calculating the trigger point for its duty to file a Schedule 13D, PX 76, so the trust's purchases could not have allowed Telco to delay disclosure of the Engle group's acquisition program. Fischel 1662-64; DX 600 at Ex. C.1.

26. As their third reason for attributing the Engle's group's profits to the trust's investments in Berkeley, plaintiffs argue that Cooper would not have agreed to purchase the Engle group's stock at a premium unless the trust agreed to sell its stock as part of the deal. An examination of the evidence concerning the Cooper transaction demonstrates that plaintiffs are wrong.

27. On August 18, 1978, the trust and the Engle group members that had purchased shares in Berkeley entered into a written agreement with Berkeley, Cooper, and certain officers and directors of those two companies. This agreement settled litigation by Engle group members against Berkeley, Cooper, and their officers, and provided that

Cooper would purchase for $7.50 per share all Berkeley stock held then held by Engle group members and the trust. PX 78; PX 59 at CR 20. The market price of Berkeley stock at the time was between $5.00 and $6.00 per share. DX 635. The agreement obligated Cooper to pay a total of $1,944,150 to the trust and members of the Engle group. Less than one-sixteenth of this amount – $118,500 – was for shares held by the trust. PX 258.

28. The agreement required every Engle affiliate that had owned Berkeley stock after August 1, 1975, including the Reliable trust, to: (a) sell all of its Berkeley stock to Cooper for $7.50 per share; (b) agree not to object to, or encourage others to object to, Berkeley's sale of its assets or repurchase of its shares prior to July 1, 1979; (c) release all causes of action against Berkeley, Cooper, and their officers and directors; and (d) refrain from acquiring any Berkeley or Cooper stock prior to July 1, 1979. PX 78. The agreement did allow Engle to acquire "a limited number" of Berkeley shares in his own name after January 1, 1979. *Id.* at 16.

29. Although the trust was a party to the settlement agreement, it was not a party to any of the underlying litigation, and never paid or was assessed any portion of the legal fees for conducting that litigation. Engle L-320, 330; Engle 1831; PX 410 at 4.

30. No witness from Cooper or Berkeley testified about whether those companies would have settled with the Engle group had the Reliable trust been unwilling to tender its shares. Both plaintiffs and defendants did offer expert opinion testimony on this issue, however. Stern testified that it is virtually unheard of for targets of hostile takeover attempts to buy out the stock of hostile shareholders at a premium unless the company regains control of all hostile shares and receives a long-term "hands-off" promise from the aggressor. PX 412 at 8. According to Stern, because Berkeley management considered the Engle

group's shares hostile, and because the trust's shares were subject to Engle's control, Berkeley would not have settled with the Engle group and paid a premium for its shares unless the trust relinquished its holdings. *Id.*; Stern 472.

31. Like Stern, Siegel testified that Cooper would not have agreed to purchase the Engle group's Berkeley stock at a premium unless it could acquire all shares under the Engle group's control, including those held by the trust. Siegel 145354. Siegel based his opinion on a belief that companies will only consummate "selective repurchase agreements" with shareholders hostile to management if the purchasers are certain of acquiring all shares under the control of the hostile group. *Id.* Siegel admitted under cross-examination, however, that a shareholder such as the trust which controlled less than one percent of a company's stock, displayed no intention of buying additional shares, and had not participated in any litigation against the company, would not constitute such a threat to management that the shareholder could command a premium for the sale of its stock. *Id.* at 1535-36.

32. Fischel testified that Cooper had no reason to insist on buying the trust's shares along with the shares of other Engle group members. According to Fischel, if every Engle group member except the trust tendered its shares and signed a hands-off agreement, the trust's resources would be too small to threaten Berkeley management and endanger the purposes of the settlement agreement. DX 600 at 12-14, 27-29; Fischel 1689-92. Matthews likewise testified that the trust's holdings of Berkeley stock were so small they posed no threat to Cooper. Matthews 2019. Moreover, he added, the trust was not a party to the litigation involving Berkeley and Cooper, and lacked the assets to buy a material amount of Berkeley stock. *Id.* Matthews testified that Cooper would have paid the Engle group the same price for its Berkeley stock regardless of whether the trust sold its shares as part of

the agreement, and that had he been advising Cooper management he would have counseled it not to insist on acquiring the trust's shares. *Id.* at 2017-20.

33. Fischel identified four factors as responsible for Berkeley's and Cooper's fear of the Engle group, and ultimately for Cooper's willingness to pay a premium to buy out the Engle group's holdings: (1) Engle's reputation for engaging in hostile takeovers, coupled with Telco's statement in its Schedule 13D that it might seek control of Berkeley in the future; (2) the Engle group's ownership of more than 10 percent of Berkeley's stock; (3) the Engle group's access to capital for further acquisitions; and (4) the lawsuits filed by members of the Engle group. Fischel 1679-80. The court finds Fischel's analysis credible, as it does his observation that the trust's investments were irrelevant to each factor. *Id.*

34. There is no evidence any member of the Engle group ordered or urged Dardick to sell the trust's Berkeley stock in conjunction with the Engle group's settlement agreement with Cooper. Minutes of directors' meetings of Telco, Telvest, and Libco suggest those companies' directors never discussed whether the trust should sell its shares pursuant to the settlement agreement. PX 59 at CR 13-24; PX 60 at 2679-86; PX 305-06. Engle L-320-21. Moreover, Engle testified that when he negotiated the price Cooper would pay for the Engle group's Berkeley stock, the parties to the negotiations did not contemplate including the trust's shares in the purchase agreement. Engle 1830-31, 1878. *See also id.* at 853. The question of the trust's participation arose only after the price had been set, when Dardick asked Cooper to buy the trust's shares. *Id.* at 1830-31; PX 410 at 4. The court considers Engle's testimony on this issue credible, and finds that Cooper did not insist on purchasing the trust's stock, but acquired it only at Dardick's request.

35. This finding is consistent with Fischel's and Matthews' analysis of the Cooper-Engle group transaction,

which is more persuasive than the analysis by plaintiffs' experts. So long as Cooper and Berkeley could extract a promise from Engle not to interfere with their planned transactions and not to give the trust access to funds for its own takeover attempt promises Engle had no reason to withhold and a strong financial incentive to make – Cooper and Berkeley could not fear the trust.

36. Regardless of whether the trust could have scuttled the agreement among Berkeley, Cooper, and the Engle group by refusing to participate, it had no reason to do so. The agreement left the trust with a profit of 66 percent on its Berkeley holdings. PX 78; PX 258. It was not in the trust's interest to reject a premium of approximately $1.50 per share above the market price and retain its substantial investment in Berkeley. Fischel 1689. Indeed, particularly because that investment was speculative and inadequately diversified, Dardick's decision to rid the trust of the investment was justifiable.

37. If it is not already apparent, this is an appropriate place to note that the court found Fischel, defendants' principal expert witness on the issue of whether the Engle group profited by the trust's stock investments, an extraordinarily able witness in terms of the depth and breadth of his understanding of this case. The court finds his testimony highly credible and persuasive. By contrast, plaintiffs' principal expert witness, Stern, was less knowledgeable about the events underlying this litigation, and his testimony attributing the Engle group's profits to the trust's stock investments rested primarily on unsubstantiated speculation.

38. The evidence demonstrates that the trust's investments in Berkeley enabled Engle group members neither to acquire shares at a lower price nor to sell shares at a higher price than would otherwise have been possible. *See* Fischel 1661. Because the Engle group did not profit from the trust's investments in Berkeley, it could not have gained

by recycling its profits into OSI and Hickory. Accordingly, the court finds that Engle, Libco, Dardick and Zuckerman did not profit from their breaches of fiduciary duty with respect to the trust's investments in Berkeley.

OSI

39. With respect to OSI, plaintiffs argue that the Engle group profited from the trust's purchases because (a) they affected the stock price; (b) they led OSI's management to seek out a "white knight" willing to acquire the company's shares at a premium; and (c) the Brown Group, Inc. ("the Brown Group") would not have made its tender offer for OSI shares unless it had expected the trust to sell its shares. Plaintiffs also claim that the Engle group used profits attributable to the trust's OSI investments to acquire stock in Hickory. PX 412 at 9-10.

40. The first of plaintiffs' arguments – that the trust's investments in OSI benefited the Engle group by increasing (or decreasing) the price of OSI's stock fails for the same reasons as their similar argument with respect to Berkeley. The evidence shows that the trust's purchases did not increase the price of OSI stock, and that even if it did, such an increase would have hurt rather than helped the Engle group. The evidence also shows that the trust's purchases did not enable the Engle group to delay the filing of a Schedule 13D and acquire OSI stock at depressed prices.

41. As he did with Berkeley, Fischel prepared a chart comparing the daily return on OSI stock with the expected daily return on stock in comparable companies. His study establishes the absence of any statistically significant changes in the price of OSI stock on or immediately after any of the five dates when the trust purchased 12,400 of its 12,500 shares March 22, 1978, when the trust purchased 1400 shares; March 23, when it purchased 2500 shares; March 29, when it purchased 2100 shares; March 30, when it purchased 1500 shares; and March 31, when it purchased 4900 shares. DX 600 at Ex. E; PX 259. Fischel's study also

finds no statistically significant change in OSI's stock price on any of the five trading days after Telco publicly disclosed the trust's OSI holdings by filing a Schedule 13D. DX 600 at Ex. E. Fischel's study is careful and detailed in this respect, and the court accepts its conclusions as accurate.

42. Fischel did find a statistically significant change in OSI's daily return on April 11, 1978, when the trust purchased its final 100 shares of OSI, and on the following day, April 11. *Id.* OSI's stock traded at $6.750 on April 10, $7.375 on April 11, $7.875 on April 12, and $7.750 on April 13. Id. Although Fischel's study offers no explanation for this jump in the stock price, the court finds it impossible to suppose the trust's purchase of a paltry 100 shares had anything to do with it – particularly when earlier and much larger purchases by the trust had no discernable impact on OSI's stock price.

43. Examination of a graph of OSI's stock price between March 1, 1978 and July 2, 1979 adds nothing to Fischel's statistical analysis. OSI's stock price rose only slightly (from $5.875 to $6.250, DX 600 at Ex. E) over the course of the trust's first five purchases, and the trust's final, negligible purchase came roughly in the middle of a weeklong run-up of the stock price. DX 636. The chart also fails to show any unusual stock price movement around the time Telco filed its Schedule 13D. *Id.*

44. By the last of the trust's purchases of OSI stock on April 11, 1978, the Engle group had acquired less than ten percent of the OSI stock it would eventually buy. Fischel 1696; PX 259. Even if the trust's investments in OSI had increased the market price of OSI stock – a proposition the court rejects – such an increase therefore would have harmed rather than helped the Engle group.

45. The trust's OSI purchases did not enable the Engle group to prolong the secrecy of its acquisition program by delaying the filing of a Schedule 13D, since members of the Engle group counted the trust's shares with their own

in determining when their holdings were sufficiently large to trigger the filing requirement. DX 600 at Ex. C; Siegel 1555-56.

46. Plaintiffs' remaining arguments linking the Engle group's OSI profits to the trust's investments are that the trust's purchases prompted OSI management to seek a "White Knight," and that the Brown Group would not have made its tender offer for OSI stock unless it expected the trust to tender its shares. Both arguments are groundless.

47. OSI management did not regard the Engle group as hostile until well after the trust completed its purchases. Engle and investment consultant Charles Newbill visited OSI's Denver headquarters in early May, 1978 and met with the company's management to discuss Engle's interest in investing in OSI. 727 F.2d at 120; Engle L-201; Newbill L-687. This encounter was friendly, Newbill L-687, and in a cab ride to the airport at the end of the visit Engle informally asked OSI's president whether OSI would consider giving the Engle group representation on its board of directors. *Id.* at L-690. OSI's president responded noncommittally. *Id.* Engle reported to Telco's board of directors on June 20, 1978 that he had not yet received a response to his informal request for representation. PX 59 at CR 14.

48. Charles Brickman, an investment banker who acted as an adviser to OSI management during 1978 and 1979, testified that sometime after Engle's visit OSI management came to believe Engle planned a hostile takeover of their company. Brinkman L-509. OSI management thereafter considered all shares in Engle's control to be hostile, and viewed the trust and its holdings as part of the Engle group. Id. at L-512. Because OSI management did not consider the Engle group hostile until well after the trust acquired its shares, those purchases in and of themselves could not have prompted OSI to seek acquisition

by a "friendly" third party.

49. OSI filed suit against various members of the Engle group on September 1, 1978, seeking an order enjoining them from acquiring additional shares and from attempting to exercise control over the company's management. PX 59 at 2628. OSI filed another suit seeking similar relief against essentially the same parties on January 29, 1979, and on February 6, 1979, Telco's investment subsidiary, Telvest, sued OSI to enjoin implementation of an anti-takeover measure. *Id.* at 2641-43. The trust was not a party to any of this litigation, and never paid or was assessed any expenses connected with it. Engle L-330; PX 410 at 4.

50. In early April, 1979, OSI proposed an agreement under which the parties would settle their litigation, OSI would buy out the Engle group's stock holdings and pay a portion of the Engle group's legal fees, and the Engle group would pledge not to acquire any more shares of OSI. PX 60 at 2723-24. The Engle group considered this offer inadequate. *Id.* at 2726.

51. The minutes of a May 22, 1979 meeting of Telvest's board of directors indicate that the Engle group was then considering a tender offer by the Brown Group to acquire all outstanding shares of OSI for $15.00 per share. *Id.* at 2729-30. At the time, OSI's stock was selling at $14.50 per share. DX 600 at Ex. E. The Brown Group publicly announced its tender offer on June 1, 1979. PX 138. Kidder Peabody & Co., an investment bank retained by OSI to help fend off a hostile takeover, played a major role in encouraging the Brown Group's bid. Brickman L-525.

52. There is no evidence that the trust's purchases of OSI shares in March, 1978 had any impact on the Brown Group's decision to make its tender offer more than a year after those purchases occurred, nor is there any evidence that the trust's purchases played a role in the decision by OSI management to seek a tender offer from a "white

knight". The trust's 12,500 shares of OSI represented less than one percent of OSI's outstanding stock at the time the Brown Group made its tender offer, PX 138, and therefore posed no threat to the Brown Group's acquisition of control over OSI. Fischel 1696-97. Moreover, in the unlikely event that the trust had rejected the tender offer, turning down a handsome profit and maintaining its imprudently large investment in OSI, the Brown Group could have forced the trust out as a shareholder by merging OSI with the Brown Group. *Id.* at 1697. Fischel testified that the same four factors responsible for Berkeley's and Cooper's decision to resist the Engle group led OSI management to seek a "white knight." Fischel 1695-96. The court accepts Fischel's explanation of the Engle group's profits on its OSI stock, as well as his conclusion that "[n]one of those factors were in any way related to the small investments by the pension trust." *Id.*

53. The Brown Group did not condition its tender offer on the trust's willingness to sell its shares of OSI; indeed, the terms of the offer required the Brown Group to purchase all tendered shares regardless of the trust's actions, so long as shareholders tendered at least 51 percent of the outstanding stock. PX 138; Matthews 2023. There is no evidence the Brown Group either expected the trust to tender its shares or cared whether it did so. Accordingly, the court finds that the Brown Group would have made its tender offer and purchased the Engle group's shares even if it had expected the trust not to sell.

54. The trust accepted the tender offer on June 26, 1979 and sold its OSI stock to the Brown Group for $15.00 per share. 727 F.2d at 121. The sale brought the trust a profit of 141 percent on its original investment. *Id.* Even if the trust's participation had been essential to consummation of the Brown Group's tender offer, it would not have been in the trust's interest to reject that offer and retain its large, undiversified investment in OSI.

55. The evidence demonstrates that the Engle group did not profit in any way from the trust's investments in OSI.

Hickory

With respect to Hickory, plaintiffs claim that the Engle group profited by (a) reinvesting proceeds derived from the trust's investments in Berkeley and OSI, PX 412 at 12; and (b) using the trust's assets in its successful effort to gain control of Hickory.

56. Because the Engle group did not profit from the trust's investments in Berkeley and OSI, it could not have gained by reinvesting such profits in Hickory. The court accordingly turns to plaintiffs' second argument, that the Engle group used the trust's assets to help it gain control of Hickory.

57. The Engle group's holdings of Hickory stock rose above 50 percent of the company's outstanding shares in late October, 1980. PX 406 (Form 8-K filed Dec. 10, 1980). The Reliable trust owned no stock in Hickory then, having sold all its shares on March 19, 1979. The trust's purchases of Hickory stock thus played no direct role in the Engle group's acquisition of control over Hickory.

58. Plaintiffs suggest that the trust's purchases may have indirectly helped the Engle group gain control of Hickory by enabling it to apply equity accounting with respect to its Hickory investments beginning in August, 1978. According to plaintiffs, this in turn increased the Engle group's financial resources and allowed additional investments in Hickory. Judge Leighton found at the first trial, however, that the trust's holdings of Hickory stock played no role in the Engle group's decision to use equity accounting, and the Seventh Circuit expressly declined to reject this finding, 727 F.2d at 132, n. 27. The evidence presented to this court is entirely consistent with Judge Leighton's determination. Although Telco did use equity

accounting with respect to its investment in Hickory (something it did not do with respect to its investments in Berkeley and OSI), it did not take the trust's stock ownership into account in doing so. Torgerson 1899-1902.

59. The Seventh Circuit advances the possibility that the trust's actions could have aided the Engle group's acquisition program by depressing the stock price – perhaps by retaining its shares while the Engle group was accumulating stock, or by selling them at a low point in the market after the success of the Engle group's acquisition program was assured. 727 F.2d at 131. Plaintiffs have not pursued this hypothesis and no evidence promotes it in this exhaustive record. The trust's retention of its Hickory stock could not have depressed the market price for the benefit of the Engle group, since purchases by an investor ordinarily tend to increase the stock price, and any increase is not offset until she sells her shares. Fischel 1662; DX 600 at 9. By retaining its stock while the Engle group was buying, the trust thus increased rather than decreased the Engle group's acquisition costs.

60. The Engle group could not have gained from the trust's sale of its shares at a low price after the success of the Engle group's acquisition program was assured; if the sale had any impact at all on Hickory's stock price it would have been negative, DX 600 at 9, and the Engle group would have gained more by lowering the stock price earlier. Moreover, the trust's sale of its shares *after* the success of Engle group's program was assured could not have contributed to the success of that program. Any theorizing about the market reaction to the trust's sale of its shares is pointless, though, in light of the fact that Hickory's stock price was unchanged during the nine market days immediately following the trust's sale of its shares. DX 600 at Ex. F.

61. Because the evidence demonstrates that the trust's investments in Hickory played no direct or indirect role

in the Engle group's acquisition of control over Hickory, and neither lowered the price at which the Engle group purchased its shares nor assisted its investment program in any other way, the court finds that the Engle group did not profit from the trust's investments in Hickory.

B. Conclusions of Law

1. Under ERISA,

> [a]ny person who is a fiduciary with respect to a plan who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by this subchapter shall be personally liable to make good to such plan any losses to the plan resulting from each such breach, and to restore to such plan any profits of such fiduciary which have been made through use of assets of the plan by the fiduciary, and shall be subject to such other equitable or remedial relief as the court may deem appropriate, including removal of such fiduciary.

29 U.S.C. § 1109(a).

2. The breaching fiduciaries – Dardick, Zuckerman, Libco, and Engle – therefore are liable to restore to the trust any losses the trust incurred as a result of their breaches of fiduciary duty, as well as any profits they made through use of the plan's assets. *Id.*; 727 F.2d at 137; *Brandt v. Grounds*, 687 F.2d 895, 898 (7th Cir. 1982). The court may require the breaching fiduciaries to disgorge their own profits only to the extent that "there is a causal connection between the use of the plan assets and the profits made by the breaching fiduciaries." 727 F.2d at 137.

3. "[T]he burden is on the defendants who are found to have breached their fiduciary duties to show which profits are attributable to their own investments apart from their control of the Reliable Trust assets." 727 F.2d at 138.

4. In determining the amount that the breaching fiduciaries must restore to the trust as a result of the trust's investments in Berkeley, OSI, and Hickory, the court "should resolve doubts in favor of the plaintiffs." *Id.* at 138-39. This ensures that the trust does not suffer simply because the breaching fiduciaries' actions have made it difficult to calculate damages. *Id.*

5. Defendants have shown that no member of the Engle group– including the four breaching fiduciaries – profited from the trust's investments in Berkeley, Hickory, and OSI. Because defendants' profits on those stocks are attributable entirely to their own resources and investments, Dardick, Zuckerman, Libco, and Engle are not liable to pay any funds to the trust as restoration of profits gained through use of the trust's assets.

6. Whether the trust lost money as a result of its investments in Hickory depends on whether the court views those investments individually or as a part of a portfolio consisting of Berkeley, OSI, and Hickory; as the court observed in its findings of fact, the former approach requires a finding of damages, while the latter requires a finding of no damages.

Black's Law Dictionary (5th ed., 1979) defines "portfolio" as follows: "[i]n investments, the collective term for all the securities held by one person or institution." *Accord, Webster's Third New International Dictionary* (1981); *The American Heritage Dictionary of the English Language* (1969). The trust's Hickory stock satisfies this definition to the extent that Hickory was simply one of three companies whose stock the trust held in the spring of 1978. But insofar as the definition of portfolio requires that the portfolio's components be acquired for *investment* purposes, the trust's purchases fall outside the definition, since the Seventh Circuit found that Dardick did not purchase Hickory stock solely for the benefit of the trust. 727 F.2d at 129-31. Because Dardick purchased Hickory's stock at

least in part for purposes other than investment, and because ERISA's goal of protecting the integrity of employee trust funds requires exacting scrutiny of the actions of breaching fiduciaries, the court declines to consider the trust's Hickory shares as part of an investment portfolio. This conclusion compels a finding that the trust's Hickory purchases damaged the trust in the amount of the difference between the trust's actual earnings from those purchases, and what the trust would have earned by making a reasonably prudent alternative investment.

7. Fischel and Matthews calculated damages to the trust from its Hickory investments in six different ways, taking as their starting points six alternative investment strategies yielding different returns. While each of these strategies would have been reasonable, neither Fischel nor Matthews nor counsel for any party suggested how the court should select the single most appropriate alternative to the trust's Hickory investments.

8. Because defendants bear the burden of proof on damages and the court must resolve all doubts in plaintiffs' favor, the court selects the most generous of the three measures of damages – all of which are reasonable – because defendants have not shown that a different measure is more appropriate. Accordingly, the court concludes that by investing trust assets in Hickory in breach of their fiduciary duties, Dardick, Zuckerman, Libco, and Engle caused damage to the trust in the amount of $6,704. This equals the difference between what the trust actually earned from its Hickory investments and what it would have earned by making a reasonably prudent alternative investment – namely, by dividing the same amount of money equally among all of Harris Bank's common stock funds.

9. Although the court has discretion to allow prejudgment interest on damage awards under ERISA, *see Katsaros* v. *Cody*, 744 F.2d 270, 281 (2nd Cir. 1984), it declines

to do so in this case for two reasons. First, had plaintiffs' counsel adopted a more realistic attitude toward the size of the potential recovery from defendants, this litigation would have ended years ago and the prejudgment interest would have been insignificant. Gil Matthews bluntly but aptly appraised plaintiffs' theories of investment-related damages: "I think this whole case is foolhardy because I can't see that the numbers here are big enough to make it worth anyone's while to pursue this. I think the legal fees and the expert fees are absurd in relation to what I view the potential award as being." Matthews 2064. An award of prejudgment interest on modest damages on issues that more reasonable counsel could have resolved years ago would unduly reward wasteful, even profligate, litigation. Second, by selecting the highest possible measure of damages, the court has conceivably compensated plaintiffs well beyond their actual loss. Adding prejudgment interest would multiply this potential munificence.

III. DELAY IN DISTRIBUTION OF TRUST ASSETS

A. Findings of Fact

1. The Restated Reliable Manufacturing Corporation Employees' Profit-Sharing Plan ("Restated Plan"), L-DX VV, incorporates the Trust Agreement for the Reliable Manufacturing Company Employees' Profit Sharing Trust ("Trust Agreement"), PX 8. L-DX VV at A. Section 9.1 of the Trust Agreement provides:

> This Trust shall terminate upon the first to occur of the following:
>
> (a) Thirty (30) days after the receipt by the Trustee of written notice of such termination from the Company;
>
> (b) The date the Company shall be judicially declared bankrupt or insolvent;
>
> (c) The dissolution, consolidation or reorganiza-

> tion of the Company, or the sale by the Company of all or substantially all of its assets without provision for continuing this Trust, except that in any such event provision may be made for the continuance of this Trust by any successor to the Company or any purchaser of all or substantially all of its assets, and in that event such successor or purchaser shall be substituted for the Company hereunder.

PX 8.

2. Section 5.6 of the Restated Plan provides in relevant part:

> The distributions of the Account provided hereunder shall be made in such one or more of the methods following as the Committee[5] in its sole discretion, may determine:
>
> (a) one lump sum payment; or
>
> (b) payments in equal monthly, quarterly, semi-annual or annual installments, over a period not exceeding ten (10) years; or
>
> (c) payments over the life of the Participant and/or his spouse.
>
> * * *
>
> Notwithstanding anything to the contrary stated in Section 5.1 through 5.6, a Participant or beneficiary, unless he shall agree to the contrary, shall be entitled to a distribution within sixty days after the close of the Year coinciding with or following the date of

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[5] The "Committee" consisted of Dardick and Zuckerman. PX 351 at 47.

entitlement.

L-DX VV. The committee determined to pay beneficiaries' interests in annual installments over a 10-year period. PX 351 at 69.

3. Section 7.2 of the Restated Plan provides:

> The Employer shall have the right at any time to discontinue its contributions hereunder and to terminate this Agreement and the Trust hereby created, by delivering to the Trustee and the Committee written notice of such discontinuance or termination.
>
> Upon complete discontinuance of the Employer's contributions, partial or complete termination of the Trust [sic] all Participants' accounts shall become fully vested, and shall not thereafter be subject to forfeiture. Upon termination of the Trust, the Committee shall direct the Trustee to distribute all assets remaining in the Trust, after payment of any expenses properly chargeable against the Trust, to the Participants in accordance with the value of such Participants [sic] accounts as of the date of such termination in cash or in property valued at fair market value as of the date of distribution and in such manner as the Committee shall determine. The Committee's determination shall be conclusive upon all parties.
>
> Upon termination, if there shall be any assets in the Trust Fund which have not been allocated to any Participant but are part of the Trust Fund, such assets shall be distributed to each Participant in the same proportion as the amount credited to the account of each Participant bears to the total of the amounts credited to the accounts of all Participants in such Trust.

L-DX VV.

4. Libco purchased 100 percent of Reliable's stock in April, 1977. 727 F.2d at 116. During 1977, customers returned large numbers of one of Reliable's products because of a design defect, and the company's sales fell. Zuckerman 469-70; Zuckerman L-456-57; P1X 58. Reliable ended the 1977 fiscal year with a loss, P1X 58, making no contributions to the profitsharing trust after March 31 of that year, L-DX III.

5. Reliable's sales again were weak in the fall of 1978, due to a sluggish market and damage to the company's reputation from the previous year's design problems. Zuckerman 480-41.

6. Zuckerman, who was Reliable's chief operating officer, Zuckerman 233, told a meeting of Libco's board of directors on August 1, 1978 that demand for Reliable's products was falling and the company had lost roughly $400,000 during the first seven months of 1978. PX 58 at CR 22-23. Reliable's poor sales and the large volume of customer returns left it with unbalanced inventories and excessive amounts of raw materials. Zuckerman at L-456-57. Zuckerman told Libco's board at the August 1 meeting that he was developing a plan for "liquefying" the company's assets by reducing inventories and converting them into finished goods that could be sold for cash, which in turn would allow Reliable to retool and reenter the market with a more suitable product mix. *Id.*; PX 58 at CR 22-23. When Zuckerman used the term "liquefying", he meant that the objective of his plan was to increase the company's liquidity – that is, to increase the amount of cash available to Reliable. *Id*; Engle 800-01. Zuckerman did not mean that he planned to liquidate the company or cease operations. *Id.* In November or December, 1978, Zuckerman decided that Reliable would produce at a high volume until it ran down its inventories, since the economies of higher volume production would enable it to produce at lower cost.

Zuckerman 484.

7. Between March, 1978 and February, 1979, Reliable borrowed $907,000 from Harris Bank and approximately $600,000 from Libco. As of February, 1979, Reliable owed a total of $655,000 to Harris Bank and $443,000 to Libco. PX 311.

8. Reliable did not earn a profit in 1978, and accordingly did not contribute money to the profit-sharing trust. L-DX XX.

9. Libco president George Contarsy, a director of Reliable, Contarsy L-388-89, told a Libco board meeting on December 28, 1978 that Reliable probably would lose between $800,000 and $1,000,000 in 1978. Zuckerman told the board Reliable was trying to work out a plan to minimize the risk of further losses and allow a reasonable return on Libco's investment. Among other options, Reliable was considering contracting out its manufacturing function. PX 58 at 2596-97. At the time, top officers of both Libco and Reliable considered Reliable a troubled but viable company.

10. Harris Bank resigned as the trust's trustee in December, 1978 because of its concern over repeated delays in obtaining proper documentation for certain of the trust's securities transactions (transactions which did not involve Berkeley, OSI, and Hickory). Meyer L-557-60. National Boulevard Bank agreed on January 2, 1979 to become the new trustee for the trust, and received its assets on February 5, 1979. PX 183.

11. On or about February 28, 1979, Reliable laid off 75 of its 81 workers, Zuckerman L-461, telling them it planned to let them know by mid-April whether or not it would recall them, PX 351 at 19. *See also* Zuckerman 336-38. The remaining workers performed office tasks, maintenance, clean-up, and shipping. Zuckerman 338; PX 29 at 308-09. Reliable's lease on its manufacturing and office facility expired in February, 1979, but the company

remained on the premises after that date, paying rent of $3000 per month. Zuckerman 357; PX 311 at Ex. 17. Although Reliable terminated its last employee sometime in the summer of 1979, it subsequently hired some former employees as independent contractors to work on an hourly basis. *Id.* No one remained on the premises after October or November, 1979. Id. at 31. The company retained its brokered sales force during this period. Zuckerman 354.

12. Despite the seriousness of Reliable's financial problems in the late winter and spring of 1979, neither Zuckerman nor Libco believed the company was beyond recovery. Zuckerman had recently revived another failing company with only a few of its employees left, Zuckerman 488, and Libco was reluctant to walk away from its more than one million dollar investment in Reliable, *Id. See also, id.* at 454-55. Zuckerman believed Reliable had two good products and at least one large customer, and that the company might survive by changing its product line, moving its plant, or eliminating its stamping operation and continuing in business as an assembly or distribution operation. *Id.* at 486-87.

13. Reliable's creditors filed an involuntary bankruptcy petition against Reliable on March 8, 1979, and on March 16, 1979 Reliable converted the proceedings into voluntary proceedings under Chapter 11. 727 F.2d at 136; PX 30; PX 25A. The bankruptcy court adjudicated Reliable a bankrupt on December 5, 1979. DX 628. Reliable's management knew that its creditors planned to file an involuntary bankruptcy petition several weeks before they actually did so. Zuckerman L-471.

14. Lawrence Hoffman, National Boulevard Bank's vice president in charge of employee benefits and the official responsible for the bank's duties as trustee of the Reliable trust, learned in February, 1979 of the lay-offs of a majority of Reliable employees. Hoffman 1265; Hirsch 1985. After consulting with the bank's counsel about the significance

of these lay-offs for distribution of the trust's assets, he told Dardick and Zuckerman that under the circumstances he would be uncomfortable making distributions to beneficiaries without a determination letter from the Internal Revenue Service ("IRS") stating that recent events had caused a termination of the trust. Zuckerman 489-90; Hoffman 1263-64. Zuckerman then called Austin Hirsch, an attorney who had previously performed work for the trust, and asked him to request such a letter from the IRS. Hirsch 1985-86. The trust retained Hirsch for this purpose on February 25, 1979. Zuckerman L-457-58; IntX 401.

15. Hirsch wrote a letter dated March 1, 1979 to the Employees' Plans Division of the IRS in Chicago. This letter informed the IRS that "[d]ue to adverse business conditions and a seasonal layoff, approximately 75 of the 81 employees participating in the Plan have been temporarily laid off as of approximately March 1, 1979. At this juncture, it is unknown whether or not Reliable Manufacturing Corporation will be in a position to re-hire these individuals wthin the next several months." PX 1. The letter went on to inquire (1) whether, assuming Reliable did not rehire a substantial percentage of its employees, there would be a partial termination of the plan, and if so, (2) whether all of the terminated employees would be fully vested and (3) whether the plan's committee "would commence distribution of accrued benefits within 60 days of the Plan Year after a service break in accordance with the Plan provisions." Hirsch concluded with a request for a conference with the IRS before any final determination. *Id.* The letter did not refer to the impending bankruptcy filings.

16. Hirsch persistently attempted to follow up on his request for a determination. On April 27, 1979 he learned that the Chicago office of the IRS had forwarded the request to Washington, and he asked for a copy of the transmittal letter. DX 625. On June 1 he asked the IRS for an expedited response to the request, and he did so again on June 13.

L-DX DD. The IRS finally acknowledged receipt of the trust's request on July 10, L-DX EE, but when Hirsch had received no further response by August 7 he wrote yet another letter seeing expedited review. L-DX FF. During the time the trust's request for a letter of determination was pending with the IRS, Zuckerman repeatedly asked Hirsch about the status of the request, in an effort to speed up distribution of trust assets to the beneficiaries. Zuckerman 486.

17. When Reliable discharged its employees in February, 1979, it did not tell them it had applied to the IRS for a determination of whether a termination had occurred, nor did it suggest that disbursement of their benefits depended in any way on action by the IRS. Zuckerman at L-468-69.

18. In early September, 1979, Hirsch finally received an oral opinion from the IRS, which he summarized in a confirming letter to the IRS dated September 6, 1979. Hirsch's letter said in part:

> Based upon the facts and circumstances set forth in the March 1, 1979 letter, you have concluded that in accordance with Regulation 1.401.6(b)(2) promulgated by the Treasury Department that a partial termination of the Reliable Manufacturing Corporation Employees Profit Sharing Plan has occurred as a result of the significant reduction in the percentage of participants in the Plan. Consequently, the amounts credited to the account of the affected employees are non-forfeitable. You provided as reference Section 401(a)(7) of the Internal Revenue Code and Section 411(d)(3) of the Employee Retirement Income Security Act of 1974.

L-DX GG. The trust subsequently withdrew its request for a determination. PX 3.

19. On September 14, 1979, Zuckerman wrote Larry Hoffman, who managed the trust's affairs for National Boulevard Bank, informing him that the IRS had found a partial termination of the trust, and that the trust's committee "desires to have a distribution made to the employees of the Trust." L-DX HH.

20. Two weeks later, on September 28, 1979, Dardick and Zuckerman asked the district court in this case to approve a release form which they proposed to send to all trust beneficiaries. (Although the Court of Appeals' opinion states that Dardick and Zuckerman sought approval of the release form on September 14, 1979, their motion for approval is dated September 28, 1978, and stamped as received on that date.) The terms of the proposed form gave beneficiaries two choices: they could receive immediate lump sum payment of vested funds if they were willing to release defendants from all liability, including liability in this action; or they could receive their vested benefits over a ten-year period, subject to an unspecified reserve for litigation expenses. 727 F.2d at 136. The district court rejected the proposed release on October 16, and instructed Dardick and Zuckerman to prepare a revised form that did not require beneficiaries to release their claims in this action. *Id.*

21. Dardick and Zuckerman then prepared a revised form which released Reliable, (along with its directors, officers, and employees), the Committee (including Dardick, Zuckerman, and their attorneys), and National Boulevard Bank from all causes of action except those raised in this case. PX 11; DX 622; L-DX YYY. The district court approved the revised form over plaintiffs' objections on November 16, 1979, and shortly thereafter Dardick and Zuckerman mailed the form and an explanatory cover letter to each plan participant. PX 11; Zuckerman 444-46.

22. Engle testified credibly that he never asked Dardick or Zuckerman to delay distribution of the trust's

assets, Engle 1841, and Zuckerman testified equally credibly that no one ever asked him to delay distribution of the trust's assets for any reason, Zuckerman 486. Defendants' actions with respect to termination of the trust and distribution of its assets were taken in good faith and not for the purpose of delaying distribution of trust assets to beneficiaries. There is no evidence defendants sought to delay distribution of trust assets in order to prolong the Engle group's control over the trust's holdings of Berkeley, OSI, and Hickory stock.

23. Even if defendants had delayed distribution of trust assets, the damages assessed in part II of this court's decision would compensate plaintiffs for any loss they suffered by reason of the delay. At all times before their distribution, trust assets were invested in money market funds, corporate bonds, and stocks (primarily Berkeley, OSI, and Hickory). *See* Meyer L-547-48, 598-600. Plaintiffs have never complained about the rates of return on the trust's money market and bond investments, and thus only could have lost money from a delay in distribution if the trust's stock investments yielded less during the delay than plaintiffs could have earned by reasonable alternative investments. During any delay in distribution the trust's Berkeley and OSI stock would have earned well above the rate of return on any other reasonable investment, however, and its Hickory stock would have earned the subpar return for which the court assessed damages in part II of this decision.

B. Conclusions of Law

1. For a profit-sharing trust to be "qualified" under § 401 of the Internal Revenue Code, 26 U.S.C. § 401, the plan of which it is a part must expressly provide that employees' benefits become nonforfeitable "upon the termination of the plan or upon the complete discontinuance of contributions under the plan." 26 C.F.R. § 1.407-6(a)(1). The plan also must provide that unless a trust

beneficiary agrees otherwise, payments to the beneficiary shall begin no later than 60 days after the close of the plan year in which the latest of three events occurs: (1) the beneficiary reaches the age of 65 or some other retirement age specified in the plan; (2) the 10th anniversary of the beneficiary's participation in the plan; or (3) termination of the beneficiary's employment. 26 U.S.C. § 401(a)(14).

2. Consistent with these requirements, the Restated Plan provides that "[u]pon complete discontinuance of the Employer's contributions, partial or complete termination of the Trust [sic] all Participants' accounts shall become fully vested, and shall not thereafter be subject to forfeiture." § 7.2. The Restated Plan also provides that "[n]otwithstanding anything to the contrary stated in Sections 5.1 through 5.6 [dealing with distributions upon retirement, death, disability, and termination of employment, as well as loans to participants and the method for paying distributions], a Participant or beneficiary, unless he shall agree to the contrary, shall be entitled to a distribution within sixty days after the close of the year coinciding with or following the date of entitlement." § 5.6.

3. Before it can decide whether defendants breached their fiduciary duties to the trust by delaying distribution of benefits, the court must determine when defendants were obliged to begin making distributions. Plaintiffs argue that the following paragraph from § 7.2 of the Restated Plan requires defendants to make lump sum distributions of benefits *immediately* after complete discontinuance of employer contributions or complete termination of the trust:

> Upon complete discontinuance of the Employer's contributions, partial or complete termination of the Trust [sic] all Participants' accounts shall become fully vested, and shall not thereafter be subject to forfeiture. Upon termination of the Trust, the Committee shall direct the

> Trustee to distribute all assets remaining in the Trust, after payment of any expenses properly chargeable against the Trust, to the Participants in accordance with the value of such Participants [sic] accounts as of the date of such termination in cash or in property valued at fair market value as of the date of distribution and in such manner as the Committee shall determine. The Committee's determination shall be conclusive upon all parties.

4. The court rejects plaintiffs' interpretation of § 7.2 for two reasons. First, nothing in the language of § 7.2 specifies a time or manner of distribution. Section 5.6, by contrast, provides generally for the time and manner of distributions, requiring the Committee to begin distributions no later than 60 days after the close of the year in which a beneficiary becomes entitled to distribution, and offering a choice of three approved methods of distribution. By its terms § 5.6 applies to *all* distributions made under the Restated Plan, and there is no reason to believe its drafters meant to give special treatment to distributions following termination of the plan.

Second, the only reason to suspect that § 7.2 might require distribution immediately after termination is its use of the word "upon" – as in "*[u]pon* termination of the Trust, the Committee shall direct the Trustee to distribute. . . ." But the Restated Plan also uses "upon" in the same way where immediate distributions clearly are not required. Even though the Restated Plan provides for distribution "[u]pon Retirement," 5.1, distribution "[u]pon the death of a Participant," § 5.2, and distribution "[u]pon termination of a Participant's employment for any reason other than retirement, death, or total disability," § 5.4(a), it is clear from § 5.6 that distributions arising from any of these events need not begin until 60 days after the end of the year in which the event occurred.

Accordingly, the court concludes that the trust was not required to begin making distributions to beneficiaries earlier than 60 days after the end of the year in which Reliable completely discontinued its contributions to the plan, or in which the plan completely terminated. The court thus must now determine the year or years in which these events occurred. It turns first to the question of when Reliable completely discontinued its contributions to the plan.

5. Although Reliable made its last contribution to the trust in March, 1977, that does not necessarily coincide with a "complete discontinuance" of contributions under ERISA and its related regulations. Whether a suspension of contributions constitutes a complete discontinuance sufficient to trigger a distribution of benefits turns on the employer's intent and on "all the facts and circumstances in the particular case." 26 C.F.R. § 1.401-6(c)(1). Because the evidence demonstrates that Reliable suspended its contributions to the profit-sharing trust after March, 1977 simply because it had no profits to share, and that it intended to remain in business and resume contributions if and when it returned to profitability, the court concludes that no complete discontinuance of contributions occurred at that time. Rather, the court concludes that a complete discontinuance of contributions occurred on or about February 28, 1979, because that is the date when a series of factors – the layoff of Reliable's production workers, the absence of specific plan by management for resuming production, and the impending bankruptcy proceedings combined to make it plain that Reliable's management had no present intent to resume contributions. *See* 26 C.F.R. § 1.401-6(c)(1).

6. Whether a termination of a plan has occurred "is generally a question to be determined with regard to all the facts and circumstances in a particular case. For example, a plan is terminated when, in connection of the

winding up of the employer's trade or business, the employer begins to discharge his employees." 26 C.F.R. 1.401-6(b)(2). Based upon the record of communications between the IRS and representatives of the trust, it is apparent that the IRS found the trust to have terminated – either partially or completely – no earlier than February 29, 1979. This court agrees with the IRS. February 28, 1979 marked the convergence of several factors relevant to whether a termination had occurred: layoffs of virtually all production workers; impending bankruptcy, management's lack of a specific plan for resuming production, and no reasonably apparent capacity for corporate survival. Accordingly, the court concludes that complete termination of the plan occurred no earlier than February 28, 1979. *Accord, Leigh* v. *Engle,* 619 F. Supp. 154, 157 (N.D. Ill. 1985) (Moran, J.) ("Termination of the Plan occurred sometime in 1979.")

7. Because there was neither a complete discontinuance of contributions nor a complete termination of the plan prior to February 28, 1979, the earliest date that the trust could have had to begin making distributions to beneficiaries was 60 days after the end of 1979 – that is, on March 1, 1980. There is no evidence or allegation that defendants delayed the start of distributions beyond March 1, 1980, so the court concludes that defendants did not breach their fiduciary duties by delaying distribution of trust assets.

8. Plaintiffs contend that defendants also breached their fiduciary duties to the trust by proposing, in September, 1978, a release form that would have allowed beneficiaries to receive lump sum distributions only if they relinquished their claims in this action. This effort, while reflecting defendants' cavalier attitude toward the trust and its beneficiaries, cannot give rise to liability for damages because it caused no harm; no beneficiary ever received the form, and defendants' proposal did not delay the start

of distributions beyond the required date of March 1, 1980.

IV. PUNITIVE DAMAGES

Conclusions of Law

1. Plaintiffs urge the court to award punitive damages against all defendants found in breach of their fiduciary duties. Although neither plaintiffs' second amended complaint nor intervenors' complaint specifically requests punitive damages, defendants have not objected to the court's consideration of this belated demand and have joined issue with plaintiffs on whether ERISA permits punitive damages, and if so whether a punitive damage award is appropriate in this case. Because the court answers the first question in the negative, it is unnecessary to consider the second.

2. The parties' proposed conclusions of law on the issue of punitive damages are sorely lacking: in support of their assertion that ERISA allows punitive damage awards, plaintiffs cite only *Russell* v. *Massachusetts Life Insurance Co.*, 722 F.2d 482 (9th Cir. 1983), which held that an individual beneficiary may maintain a claim for punitive damages against a breaching fiduciary – but which was reversed on precisely that point by the Supreme Court, *Massachusetts Mutual Life Insurance Co.* v. *Russell*, 473 U.S. 134 (1985) (individual suing on his own behalf may not recover punitive damages under ERISA). For their part, defendants simply cite *Sommers Drug Stores Co.* v. *Corrigan Enterprises, Inc.*, 793 F.2d 1456 (5th Cir. 1986), and *Pokratz* v. *Jones Dairy Farm*, 771 F.2d 206 (7th Cir. 1985), and assert without elaboration that these cases establish the unavailability of punitive damages under ERISA.

3. They do no such thing. *Massachusetts Mutual* deals only with the availability of punitive damages to individual beneficiaries; the Court explicitly refused to decide whether a plan, or an individual suing on behalf

of a plan or all its beneficiaries, can recover punitive damages. 473 U.S. at 144. Although *Sommers* does hold that punitive damages are never recoverable under ERISA, it is not from this circuit and other courts deciding the issue since *Massachusetts Mutual* have reached contrary conclusions, *see Schoenholtz* v. *Doniger,* 657 F. Supp. 899, 913-16 (S.D.N.Y. 1987); *James A. Dooley Associates Employees Retirement Plan* v. *Reynolds,* 654 F. Supp. 457, 460-61 (E.D. Mo. 1987). But see, *Powell* v. *Chesapeake & Potomac Telephone Co. of Virginia,* 780 F.2d 419, 424 (4th Cir. 1985) ERISA does not allow punitive damages). *Pokratz,* defendants' Seventh Circuit citation, is irrelevant because it merely applies *Massachusetts Mutual,* rejecting an individual beneficiary's claim for punitive damages. 771 F.2d at 210.

4. The dispute over the availability of punitive damages under ERISA turns on the interpretation of § 409(a) of ERISA, 29 U.S.C. § 1132(a)(2), which provides that anyone who breaches his fiduciary duty to a plan

> shall be personally liable to make good to such plan any losses to the plan resulting from each such breach, and to restore to such plan any profits of such fiduciary which have been made through use of assets of the plan by the fiduciary, *and shall be subject to such other equitable or remedial relief as the court may deem appropriate,* including removal of such fiduciary.

(Emphasis added.)

5. Those who find authority in ERISA for punitive damage awards rely on the underlined portion of § 409(a). They reason that punitive damages traditionally have been available in actions for equitable relief, that ERISA's legislative history evidences Congressional intent to give courts wide flexibility in fashioning remedies for fiduciary misconduct, and that the authority in 409(a) for "such other equitable or remedial relief as the court may deem approp-

riate" resembles the remedial section of the Griffin-Landrum Act, 29 U.S.C. § 412, which allows "a person whose rights . . . have been infringed . . . to bring a civil action . . . for such relief as may be appropriate" – language courts have interpreted to authorize punitive damages. *See Schoenholtz,* 657 F. Supp. at 913-16; *Dooley,* 654 F. Supp. 460-61.

6. In *Sommers* and *Powell,* the Fourth and Fifth Circuits emphasize two reasons for rejecting punitive damage awards under ERISA. First, contrary to the claims in *Schoenholtz* and *Dooley,* punitive damages are not a traditional equitable remedy. Second, ERISA's legislative history indicates that Congress intended common law trust principles to govern fiduciary relationships under ERISA, and the common law of trusts does not treat punitive damages as "equitable relief." *Sommers,* 793 F.2d at 1463-64; *Powell,* 780 F.2d at 424.

7. *Sommers* and *Powell* are persuasive. The common law of trusts generally does not allow punitive damages, and makes exceptions only in cases of extraordinary fiduciary disloyalty or malicious conduct, neither of which is present here. G. Bogert & G. Bogert, *The Law of Trusts and Trustees* § 862, at 39-41 (2d ed. 1982); *Restatement (Second) of Trusts* 205 (1959). Moreover, while it is true courts have construed the Landrum-Griffin Act to allow punitive damages for breach of a union's duty of fair representation "where the union or its officials have acted with malicious intent or at least reckless and wanton indifference to the plaintiff's rights," *Quinn* v. *DiGiulian,* 739 F.2d 637, 648-49 (D.C. Cir. 1984) (collecting cases), courts have construed another employee-protection statute lacking specific remedial provisions, the Railway Labor Act, 45 U.S. § 151 *et seq.,* to preclude punitive damage awards, *International Brotherhood of Electrical Workers* v. *Proust,* 442 U.S. 42 (1979).

8. Congress meant courts to have considerable dis-

cretion in fashioning remedies for breaches of fiduciary duty under ERISA, but the legislative history suggests discretion limited by the bounds of common law, not judicial imagination. The common law of trusts does not make punitive damages generally available as a remedy for breach of fiduciary duty absent extraordinary misconduct, and there is no basis for reading such a remedy into ERISA. The court rejects plaintiffs' request for punitive damages.

V. ATTORNEYS' FEES

A. Findings of Fact

1. Section 11.1 of the Trust Agreement provides:

> The Trustee shall not incur any personal liability in connection with any act done or omitted to be done in good faith and with reasonable care and prudence in the administration of the Trust, and shall be indemnified and saved harmless by the Company, or from the Trust Fund, or both, from and against all liability to which the Trustee shall be subjected by reason of any such act or conduct, including all expenses reasonably incurred in its defense if the Company fails to provide such defense.

PX 8. Section 6.4 of the Restated Plan contains a similar provision.

2. Section 1.6 of the Restated Plan provides:

> Unless otherwise determined by the Employer, the members of the Committee shall serve without compensation for services as such, but all expenses of the Committee may be paid by the Employer. Such expenses shall include any expenses incident to the functioning of the Committee, including, but not limited to, fees of accountants, counsel, and other specialists, and

> other costs of administering the Plan. In the event that the expenses are not paid by the Employer, then such expenses shall be reimbursed by the Trustee.

L-DX VV. Reliable – "the Employer" – did not pay the legal fees and other expenses of Dardick and Zuckerman in this litigation, *see* IntX 418-20; 619 F. Supp. at 159, so the trust did so pursuant to § 1.6 of the Restated Plan and § 11.1 of the Trust Agreement, *id.*; PX 8; L-DX VV.

3. Nothing in either the Trust Agreement or the Restated Plan authorizes the trust to reimburse Reliable, Libco, or the directors of those companies for legal fees incurred in connection with administration of the plan. PX 8; L-DX VV.

4. Section 9.2 of the Trust Agreement provides in part:

> Upon termination of this Trust the Trustee shall first reserve such reasonable amounts as it may deem necessary to provide for the payment of any expenses then or thereafter chargeable to the Trust Fund. Subject to such reserve, the balance of the Trust Fund shall be liquidated and distributed by the Trustee to or for the benefit of the employees or former employees of the Company, or their beneficiaries, as directed by the Company."

PX 8. The trust retained a reserve of approximately $100,000 and distributed the remainder to plan participants during the several months following approval of the revised release form. IntX 418.

5. Approximately $80,000 remained in the trust on June 27, 1985, when Judge Moran, before whom this case was then pending, determined that continued retention of this amount was unnecessary and ordered the trust to distribute $60,000 to beneficiaries within 21 days. *Leigh* v. *Engle,* 619 F. Supp. 154, 159 (N.D. Ill. 1985).

B. Conclusions of Law

1. "[I]ndemnification for legal fees when a breach of trust has been established, though perhaps provided for by the trust agreement, is not allowed under ERISA." 619 F. Supp. at 159. Nothing in ERISA prohibits a trust from indemnifying its fiduciaries for legal expenses unrelated to breaches of their duties, however, and § 1.6 of the Restated Plan requires the trust to reimburse Committee members for their legal expenses when Reliable fails to do so, as it has in this case.

2. It follows that Dardick and Zuckerman are entitled to reimbursement from the trust (or more accurately, to retain funds advanced by the trust) for legal expenses not attributable to their fiduciary violations. Unfortunately, it is difficult to identify these expenses with precision. In one sense their legal expenses are entirely their own fault, since plaintiffs never would have filed this suit had Dardick and Zuckerman not made the mistake of investing trust assets in Berkeley, OSI, and Hickory. On the other hand, despite the fact that Dardick and Zuckerman neither profited personally from the trust's investments nor delayed the distribution of trust assets, they have had to spend considerable time and money refuting ill-considered allegations of such wrongdoing.

3. Plaintiffs have prevailed against Dardick and Zuckerman to the extent of establishing that they breached their fiduciary duties by investing trust assets in Berkeley, OSI, and Hickory, and that this breach caused the trust a loss of $6,704 of its Hickory investment. Because ERISA bars a trust from indemnifying breaching fiduciaries for legal expenses attributable to their breaches, Dardick and Zuckerman may not receive trust assets to defray legal expenses incurred in responding to plaintiffs' successful "wrongful investment" claim.

4. Plaintiffs' remaining claims against Dardick and Zuckerman – that they profited from the trust's stock

investments and delayed distribution of its assets – are a different matter. These unsuccessful claims turn on facts that have little in common with those at issue in plaintiffs' successful wrongful investment claim.

5. Proving that Dardick and Zuckerman wrongly invested trust assets required plaintiffs to retrace the Engle group's investment program and point out the conflict of interest that arises when a fiduciary makes speculative investments in companies in which his employer is simultaneously acquiring significant financial interests. To establish that this misconduct caused the trust's loss on its Hickory investments, plaintiffs had only to show that prudent alternative investments would have yielded higher returns.

By contrast, plaintiffs' claim that Dardick and Zuckerman personally profited from the trust's investments turns on price movements in Berkeley, OSI, and Hickory stocks, on the circumstances surrounding the trust's (and the Engle group's) sale of those stocks, and on expert testimony about possible economic or market relationships between the trust's investments and the Engle group's profits. Plaintiffs' unsuccessful claim that Dardick and Zuckerman delayed distribution of trust assets is factually even more remote from plaintiffs' wrongful investment claim, turning on the circumstances surrounding Reliable's business decline and the trust's efforts to secure a letter of determination from the IRS.

6. Because plaintiffs' two unsuccessful claims against Dardick and Zuckerman are factually and legally distinct from their lone successful claim against those defendants, ERISA does not bar the trust from paying the legal expenses that Dardick and Zuckerman incurred in refuting those claims, pursuant to § 1.6 of the Restated Plan. *See Hensley* v. *Eckerhart*. 461 U.S. 424 (1983)(in awarding statutory attorneys' fees to plaintiffs prevailing on some but not all claims, courts may award fees attributable to

pursuit of an unsuccessful claim only if that claim shares a common core of facts and a related legal theory with a successful claim); *Spanish Action Committee of Chicago* v. *City of Chicago,* 811 F.2d 1129, 1133 (7th Cir. 1987).

7. In holding that Dardick and Zuckerman are entitled to reimbursement from the trust for their legal fees in defending against plaintiffs' "illicit profit" and "delay damages" claims, but not against their "wrongful investment" claim, the court is aware of the difficulty of attributing each dollar of legal costs to one claim or another. Because ERISA prohibits trusts from reimbursing the legal expenses of breaching fiduciaries, and Dardick and Zuckerman did breach their fiduciary duties in one respect, they must bear the burden of demonstrating that any legal expenses for which they seek reimbursement are attributable solely to plaintiffs' unsuccessful claims.

8. Nothing in the Trust Agreement or Restated Plan authorizes the trust to pay the expenses of Libco, Engle, Telco, or Telvest in this litigation, and they must reimburse the trust for any expenditures made on their behalf. All issues relating to these reimbursements should, of course, be resolved before any attorneys' fees are paid out.

9. Because plaintiffs did not prevail on any of their claims against National Boulevard Bank, the bank is entitled to complete reimbursement of its legal expenses from the trust under § 11.1 of the Trust Agreement and # 6.4 of the Restated Plan.

10. In addition to determining the trust's responsibility for defendants' attorneys' fees, the court has discretion to award attorneys' fees to any party, 29 U.S.C. §1132(g)(1). The exercise of this discretion should depend on:

> (1) the degree of the opposing parties' culpability or bad faith; (2) the ability of the opposing parties to satisfy an award of fees; (3) whether an award

> of fees against the opposing parties would deter others from acting under similar circumstances; (4) whether the parties requesting fees sought to benefit all participants and beneficiaries of an ERISA plan or to resolve a significant question regarding ERISA; and (5) the relative merits of the parties' positions.

727 F.2d at 139 n. 39. *Accord, Bittner* v. *Sadoff & Rudoy Industries,* 728 F.2d 820, 828-31 (7th Cir. 1984). The court also must bear in mind that "[W]here an ERISA beneficiary substantially prevails on the merits of his or her claim, an award of fees with respect to such a claim against the party in question would almost always be an abuse of discretion." *Id.* at 140.

11. The court already has noted that plaintiffs' claim against Dardick, Zuckerman, Libco, and Engle for improperly investing trust assets is factually and legally distinct from their claims that those defendants profited by the trust's stock investments and that all defendants improperly delayed distribution of trust assets. Because the three claims are distinct, and because plaintiffs prevailed on the first but not the latter two claims, it is appropriate to consider them separately for the purpose of determining whether to award attorneys' fees under § 1132(g). *See Hensley, supra.*

12. Applying the five-part test set out by the Court of Appeals in this case, there is good reason to award attorneys' fees to plaintiffs for their successful claim that Dardick, Zuckerman, Libco, and Engle breached their fiduciary duties by investing trust assets as they did. (1) Dardick, Zuckerman, Libco, and Engle were grossly negligent in investing a substantial portion of the trust's assets in three speculative stocks. (2) The four breaching fiduciaries have the resources to pay a fee award and are better able than plaintiffs to bear this cost. (3) An award of attorneys' fees to prevailing plaintiffs will tend to deter

similar fiduciary misconduct in the future. (4) Plaintiffs (or at least intervening plaintiffs) brought this lawsuit on behalf of all plan participants, not merely for individual gain. (5) The liability of the four breaching fiduciaries is not a close question; even minimal reflection should have led them to realize it was unlawful to invest 30 percent of the trust's assets in three speculative stocks.

13. There is less reason to award attorneys fees to defendants for the two claims on which they prevailed. (1) Although plaintiffs were wrong in claiming that defendants profited by the trust's stock investments and unlawfully delayed distribution of its assets, plaintiffs did not litigate in bad faith. The circumstances of defendants' misconduct could have fostered a reasonable suspicion that the breaching fiduciaries had acted to further their own interests at the expense of the trust. (2) Until their termination by Reliable, most of the plaintiffs were factory workers with modest wages. Ordering them to pay attorneys' fees for the claims on which defendants prevailed could cause substantial hardship, while there is no evidence defendants are unable to pay their own fees. (3) An award of attorneys' fees to defendants might deter future suits in circumstances where defendants' liability is not a foregone conclusion, since plaintiffs naturally would be reluctant to risk assessments of attorneys' fees. This would be inconsistent with the remedial purposes of ERISA. (4) Defendants' successful defense of the claims against them did not benefit the plan, and an award of attorneys fees would further deplete the trust's assets. (5) Although defendants' position on the merits of plaintiffs' delay damages and illicit profits claims was distinctly stronger than plaintiffs' position on those claims, plaintiffs did not litigate in bad faith.

14. Determining with precision the portion of plaintiffs' attorneys' fees attributable to their wrongful investment claim would be a difficult and time-consuming task

– particularly, as Judge Moran so aptly noted, "[g]iven the proclivity in this case . . . for everything to escalate into a pierhead brawl," 619 F. Supp. at 159. Because extended litigation over attorneys' fees will only drain the trust, the court chooses to approximate the correct fee award by ordering defendants to pay plaintiffs' legal fees through the date of the Seventh Circuit's decision but no further. The litigation leading up to that decision established the only significant legal principles to arise from this lawsuit, and also resolved the principal factual issues on which plaintiffs prevailed. Plaintiffs have accomplished little since then other than further depleting the trust's assets by forcing its fiduciaries to incur reimbursable attorneys' fees. Awarding attorneys' fees to plaintiffs for this most recent portion of the case would reward litigation that was ill-conceived, often poorly executed, and fractious.

15. An award of legal fees for the prior stages of the case is entirely appropriate, however. Plaintiffs established then that Dardick and Zuckerman breached their fiduciary duties with respect to the trust's investments, and plaintiffs' success before the Seventh Circuit made almost inevitable this court's subsequent finding that Libco and Engle likewise breached their fiduciary duties. Plaintiffs also made it plain in the prior stages of this litigation that what Dardick, Zuckerman, Libco, and Engle did is intolerable; they played roulette with the retirement funds of employees who worked for years at modest wages, relying on defendants' pledge to safeguard their pensions. The fact that defendants' gamble paid off in this instance renders their conduct no more savory. If other fiduciaries roll the same dice with other trust funds it is inevitable that someday, somewhere, employees will lose benefits they had counted on for their retirement. Perhaps the defendants in this case are too young, too wealthy, and too comfortable to have contemplated the enormity of the risk they took, and the human suffering so narrowly averted. Because ERISA does not allow punitive damages, an award of attorneys' fees

under 29 U.S.C. § 1132(g) is the court's only means to deter similar misconduct in the future.

16. Accordingly, pursuant to 29 U.S.C. § 1132(g) the court orders Dardick, Zuckerman, Libco, and Engle to pay the reasonable attorneys' fees incurred by counsel for plaintiffs prior to issuance of the Seventh Circuit's amended decision on March 20, 1984. Because the parties have not raised the issue, the court does not consider the allocation between plaintiffs and intervening plaintiffs of its award of attorneys' fees to "plaintiffs".

V. CONCLUSION

Perhaps only Charles Dickens could savor this litigation. For nearly a decade now, the parties have fought bitterly over the Reliable trust, the only noticeable effect being the steady diminution of its assets. The advocacy has been harsh and often vituperative: lawyers have accused each other of personal wrongdoing, discovery disputes continued through the last day of trial, and shouting matches have broken out. If it were possible to bottle the contempt, even hatred, which the lawyers and parties feel for one another, there would be enough to sustain a small civil war for months. The great length and extraordinary difficulty of this litigation owes much to the depth of the combatants' animosity.

Plaintiffs struggle mightily to portray defendants as evil capitalists who sought to deprive dedicated workers of their pension benefits. The record simply does not support such a conclusion. While the four breaching fiduciaries were deplorably cavalier and vincibly oblivious to the chasm between investments appropriate for a pension fund and those appropriate for a venture capital fund, the evidence clearly establishes that they neither profited nor intended to profit by the trust's investments, and did not seek to delay distribution of its assets. It should have been apparent to plaintiffs' counsel early in the present phase of this litigation that while Dardick, Zuckerman, Libco, and Engle

did breach their fiduciary duties by improperly investing the trust's assets, this misconduct did not significantly damage the trust or benefit the Engle group. Counsel's deep emotions may have obscured their view of the merits.

In summary, the court concludes as follows: (1) Libco and Engle breached their fiduciary duties by failing to adequately supervise Dardick's and Zuckerman's investments of trust assets; (2) Dardick's, Zuckerman's, Libco's, and Engle's breaches of fiduciary duty with respect to the trust's investment in Hickory damaged the trust in the amount of $6,704, and they must restore that amount to the trust; (3) none of the defendants profited by the improper investment of trust assets; (4) none of the defendants breached their fiduciary duties by delaying the distribution of trust assets to beneficiaries; (4) Dardick and Zuckerman are entitled to reimbursement from the trust for expenses that they can show are attributable solely to their defense against plaintiffs' claims that they (a) personally profited from the trust's stock investments, and (b) delayed the distribution of trust assets; (5) National Boulevard Bank is entitled to reimbursement from the trust for all of its expenses in this litigation; and (6) Dardick, Zuckerman, Libco, and Engle must pay the reasonable attorneys' fees incurred by counsel for plaintiffs and intervening plaintiffs until issuance of the Seventh Circuit's amended decision on March 20, 1984.

ENTER:

/s/ BRIAN BARNETT DUFF

BRIAN BARNETT DUFF, JUDGE
UNITED STATES DISTRICT COURT

DATE: August 27, 1987

United States District Court

NORTHERN DISTRICT OF ILLINOIS

Eastern Division

Charles W. Leigh, et al. **JUDGMENT IN A CIVIL CASE**

v.

Clyde W. Engle, et al.

CASE NUMBER: 78 C 3799

☐ **Jury Verdict. This action came before the Court for a trial by jury. The issues have been tried and the jury has rendered its verdict.**

☒ **Decision by Court. This action came to trial or hearing before the Court The issues have been tried or heard and a decision has been rendered.**

IT IS ORDERED AND ADJUDGED that (1) Libco and Engle breached their fiduciary duties by failing to adequately supervise Dardick's and Zuckerman's investments of trust assets; (2) Dardick's, Zuckerman's, Libco's, and Engle's breaches of fiduciary duty with respect to the trust's investment in Hickory damaged the trust in the amount of $6,704, and they must restore that amount to the trust; (3) none of the defendants profited by the improper investment of trust assets; (4) none of the defendants breached their fiduciary duties by delaying the distribution of trust assets to beneficiaries; (5) Dardick and Zuckerman are entitled to reimbursement from the trust for expenses that they can show are attributable solely to their defense against plaintiffs' claims that they (a) personally profited from the trust's stock investments, and (b) delayed the distribution of trust assets; (6) National Boulevard Bank is entitled to reimbursement from the trust for all of its expenses in this litigation; and (7) Dardick, Zuckerman, Libco, and Engle must pay the reasonable attorneys' fees incurred by counsel for plaintiffs and intervening plaintiffs

until issuance of the Seventh Circuit's amended decision on March 20, 1984.

August 27, 1987
Date

H. STUART CUNNINGHAM
Clerk

/s/ CLAUDIA M. FLAGG
(By) Deputy Clerk
Claudia M. Flagg

In The United States District Court For the Northern District of Illinois Eastern Division

CHARLES W. LEIGH and ERVIN F. DUSEK,

Plaintiffs,

GEORGE JOHNSON, ELEANOR MADSEN, et al.,

Intervening Plaintiffs,

vs.

CLYDE WM. ENGLE, NATHAN DARDICK RONALD ZUCKERMAN, LIBCO CORPORATION, TELCO MARKETING SERVICES, TELVEST, NATIONAL BOULEVARD BANK, and the RELIABLE EMPLOYEES' PROFIT SHARING PLAN TRUST

Defendants.

No. 78 C 3799

MEMORANDUM AND ORDER

After an extended bench trial Judge Leighton entered 23 pages of findings of fact and conclusions of law on November 18, 1982. Upon appeal, the Court of Appeals issued a 28-page modified opinion in March 1984. *See Leigh v. Engle,* 727 F.2d 113 (7th Cir. 1984). That opinion affirmed in some respects, reversed in others, and vacated and remanded for further proceedings, with costs to be borne equally by the parties. Upon the commencement of those further proceedings before this court we requested the

assistance of the parties in fashioning a damages measure. That assistance was not forthcoming in any meaningful way, and this court detailed its concerns in October 1984 and again asked for assistance. Again the parties have been of little help, apparently not one of them seem to be able to accept what this court has accepted as the mandate from the Court of Appeals. Indeed, the most recent effort has been that of the intervenors seeking clarification from the Court of Appeals. The intervenor asked the Court of Appeals to "clarify" its opinion by adopting the intervenors' position on damages, a position this court believed the appellate decision had clearly rejected. The Court of Appeals declined. This action's troubled history continues, and it obviously is not going to end unless this court delineates the issues as we see them and, to the extent it can do so without further "assistance," acts upon them.

The principal battle is over what recovery there may be from liable fiduciaries because of their involvement in three investments. Two defendants have been found liable for damages, if any. Whether two other defendants are liable remains a factual dispute to be resolved after an evidentiary hearing.

A second area of contention relates to a reserve fund. The Court of Appeals directed this court to consider "at the first opportunity the desirability of an immediate distribution of all remaining assets...." The remaining assets in hand, however, are approximately $80,000, less than 10 per cent of the distribution long since made, and the plaintiffs and intervenors have made it abundantly clear that the remaining assets from their perspective are closer to $250,000 to $300,000, after the return of attorneys' fees and expenses to the fund. But that perception raises legal and factual questions which need to be addressed, which will be addressed herein, and which. have been virtually ignored or, in this court's view, erroneously perceived by the parties.

The third major area of dispute is whether distribution was improperly delayed; whether, if so, any damage resulted; and, if so, which of the defendants are liable for those damages and to what extent. There are, as well, other issues which have been less central to the disputes.

I. Reserve Fund

We turn, first, to the reserve fund issues. No one disputes that some of the $80,000 can be distributed. Plaintiffs and intervenors contend that the assets vested in the beneficiaries upon termination were thereupon non-forfeitable. Accordingly, even in the absence of a breach of fiduciary obligations or bad faith the Plan thereafter could pay nothing for expenses of whatever nature. Defendants contend that the trust permits a reserve, that such a reserve is necessary to pay ongoing litigation and administration expenses, that it has already been finally determined that any breaches of fiduciary duties were despite their good faith, and that such litigation expenses are therefore reimbursable from the trust pursuant to Sec. 11.1 of the Plan, which indemnifies the fiduciaries from liability for "any act done or admitted to be done in good faith and with reasonable care and prudence," including "all expenses reasonably incurred in its defense." This court believes both positions to be in error.

Termination of the Plan occurred sometime in 1979. Upon termination, pension rights vest, and, as vested rights, are non-forfeitable, as defendants admitted in their September 6, 1979 letter to the Internal Revenue Service. A non-forfeitable pension right is defined as one which is "unconditional, and which is legally enforceable against the Plan." 29 U.S.C. § 1002(19). A non-forfeitable pension right, however, is not necessarily a right to a recipient's percentage of the total fund. *In Alessi v. Raybestos-Manhattan, Inc.*, 451 U.S. 504 (1981), the Supreme Court stated clearly that the amount considered non-forfeitable must be defined by all the provisions of the Plan. "[T]he

statutory definition of 'non-forfeitable' assures that an employee's claim to the protected benefit is. legally enforceable, but it does not guarantee a particular amount or method for calculating the benefit." Id. at 512. The court, in *Alessi* asked and answered a key question. "[W]hat defines the content of the benefit that, once vested, cannot be forfeited? ERISA leaves this question largely to the private parties creating the Plan." Id. at 511. Thus, this court must look to the trust plan to determine what distributions the beneficiaries should receive. The Pension Plan provisions are determinative respecting reserves, except when they conflict with specific ERISA provisions. *Blackmar v. Lichtenstein,* 603 F.2d 1306, 1309 (8th Cir. 1979).

Section 9.2 of the Trust Agreement provides that, before distribution after termination, the trustee "shall first reserve such reasonable amounts as it may deem necessary to provide for the payment of any expenses then or thereafter chargeable to the trust fund." Attorneys' fees have been withheld as chargeable to the trust fund pursuant to Sec. 11.1 Even though the trustees were found to have breached their fiduciary duties, the Seventh Circuit did not overturn Judge Leighton's finding of good faith. *See* 727 F.2d at 124; Finding of Fact 23. We can, therefore, assume good faith has been found and defendants, according to the Plan, may possibly be entitled to be indemnified and reimbursed for any liability assessed or attorneys' fees owed (although it is difficult to square a breach of trust with "reasonable care and prudence").

The central question, largely ignored by the parties, is whether such indemnification is allowed under ERISA. Indemnification from liability for breach of fiduciary duty by a trust is not allowed under ERISA. 29 U.S.C. § 1110(a). *See Chicago Board of Options Exchange, Inc. v. Connecticut General Life Insurance Co.,* 713 F.2d 254, 259 (7th Cir. 1983). It has also been found that indemnification for

attorney's fees, even where liability has not attached, is also not allowed. *See Donovan v. Cunningham,* 541 F.Supp. 276, 289 (S.D. Tex. 1982), *modified on other grounds* 716 F.2d 1455 (5th Cir. 1983).

Defendants, quite naturally, rest entirely on the Plan language. Their position might have considerable merit if this were a question of indemnification of a corporate director of a commercial enterprise, where such indemnification is often authorized by state statute. Arguably, indemnification might be permissible under the general law of trusts on the ground that the fiduciaries acted in good faith and the investments in fact benefited the trust. *See generally* G. Bogert, The Law of Trust and Trustees, § 871, n.83 (2d Ed. 1981); *Craven v. Craven,* 407 Ill. 252, 95 N.E.2d 489 (1950). We are dealing here, however, with indemnification of legal expenses of a fiduciary of a trust fund subject to ERISA, when there has been a determination of a breach of fiduciary duty.

In an advisory opinion dated September 9, 1977, the Department of Labor commented on a provision which indemnified trustees for their legal expenses and allowed for payment in advance of the final disposition. The Department found that Sec. 1110(a) did not forbid such advances as long as the fund obtains a written legal opinion from independent legal counsel that, based on review of the relevant facts, the acts in question did not constitute breach of a fiduciary duty. *See* Department of Labor Advisory Opinion, Ref. No. CA-3588(a) (Sept. 9, 1977). This finding indicates that indemnification for legal expenses, after a finding of breach of fiduciary duty, is not allowed and any advances made would have to be returned.

Such a result has been reached with regard to the Labor Management Reporting and Disclosure Act, 29 U.S.C. § 401 *et seq. In Morrissey v. Segal,* 526 F.2d 121 (2d Cir. 1975), the court ordered defendants to reimburse the fund for legal fees advanced during an unsuccessful defense to

a breach of fiduciary duty claim. The court found that allowing indemnification for fees "would undermine both protection to union members and deterrence of union officials intended by [the Act]. *Id.* at 126. *See McNamara v. Johnston,* 522 F.2d 1157, 1167 (7th Cir. 1975), *cert. denied,* 425 U.S. 911 (1976) (allowing repayment for legal fees only if defendants prevail). The policies underlying the treatment of pension funds under the LMRDA and ERISA are similar and the provisions in 29 U.S.C. §§ 1109 and 1110 seem to confirm Congress' intent to keep legal fee policies the same for both acts as, unlike the general law of trusts, there are no exceptions for liability of a trustee who, in breaching his trust, acts in good faith and benefits the fund. Accordingly, the court finds that indemnification for legal fees when a breach of trust has been established, though perhaps provided for by the trust agreement, is not allowed under ERISA.

That does not, however, end the matter. Whether or not the fiduciaries will be successful in defending against the unresolved claims has yet to be determined. The advancement of legal expenses to them for defense against those claims, as the Department of Labor advisory opinion indicates, is an entirely different matter from the question of ultimate liability for legal expenses. *And see Central States, Southeast and Southwest Areas Pension Plan Fund v. American National Bank and Trust Co.,* No. 77 C 4335, slip op. at 6 (N.D. Ill. 1979). That issue has not been addressed by the parties. Whether or not an advancement is proper, however, an initial and continuing reserve for reimbursement in the event of exoneration was and remains proper. To the extent that funds have been or will be necessary to defend against unresolved claims, they cannot be available for distribution to the beneficiaries until and unless there is a liability determination adverse to those defendants.

That raises one of several related factual issues.

Plaintiffs and intervenors appear to treat legal expenses as some sort of fungible mass. They are not. The lawsuit was against several defendants and raised several issues. Two defendants, Telco Marketing Services, Inc. and Televest, Inc., were apparently represented by a law firm which was not paid by the Plan, nor is there any apparent basis why they could have been. Libco and Engle were also apparently represented by this firm, and the expenses of their defense have not, apparently and for similar reasons, been paid by the Plan. The Plan and three fiduciaries have had their legal expenses advanced by the Plan. They represent that half of those expenses have been borne by an insurance carrier, something specifically sanctioned by ERISA so long as there is recourse. 28 U.S.C. § 1110. Moreover, one of the fiduciaries has not been found liable for anything and the other two have been found liable on only one of the central issues. In those circumstances, some apportionment of defense costs is necessary before an order is entered directing reimbursement of the Plan.

That apportionment is somewhat in the nature of an accounting and could very well be referred to a magistrate for a recommendation and report. Given the proclivity in this case, however, for everything to escalate into a pierhead brawl, this court questions the desirability of initiating such a proceeding when subsequent events, *i.e.*, a determination of liability on other issues, could obviate the need for any such proceeding at all.

That leaves, then, approximately $80,000 presently in the reserve fund, a portion which is immediately distributable to the beneficiaries, and they have waited a long time. It cannot be used to pay the further legal expenses of defendants Dardick and Zuckerman respecting the damages issues left after conclusive determination of the breach of fiduciary duty issues arising from the investments. It may, however, be available to pay their and National Boulevard Bank's legal expenses in defending

against other charges, depending on the outcome. This court is of the view, based on its present knowledge of the case, that those other issues are not likely to be so complex that they require an inordinate amount of legal effort. In those circumstances the court directs that $60,000 be distributed to the beneficiaries within 21 days and the balance be held for possible reimbursement of legal expenses and for the incidental expenses of maintaining the modest balance in trust.

II. Remedy

This court now faces the "formidable task of finding an appropriate measure of damages, if any, with regard to all defendants found to be liable as fiduciaries." *Leigh v. Engle*, 727 F.2d at 137. The remedy statute for breach of fiduciary duty, 29 U.S.C. § 1109, gives two bases for liability. First, fiduciaries are liable for "any losses to the Plan resulting from" any breaches. Second, fiduciaries must "restore to such Plan any profits of such fiduciary which have been made from use of assets of the Plan by the fiduciary."

A. Losses

Defendants argue that because the plaintiff suffered no losses from the transactions involved, they cannot be liable for damages under the first part of Sec. 1109. The Second Circuit recently dealt with this question and disagreed. In *Donovan v. Bierwith*, 754 F.2d 1049 (2d Cir. 1985), the court found liability for losses under Sec. 1109 even where the trust made a profit on the transaction. The court found the notion of opportunity cost fixed within trust law and determined that a trustee is liable for "any profit which would have accrued to the trust estate if there had been no breach of trust." *Id.*, slip op. at 11, *quoting* Restatement (Second) of Trusts, § 205(c) (1959). *See also Eaves v. Penn*, 587 F.2d 453, 463 (10th Cir. 1978). The court stated:

> In view of the intent expressed by in providing for the recovery of "losses," in the absence of evidence of congressional attempt to penalize, as such, violations of section [1109], we hold that the measure of loss applicable under ERISA, section [1109], requires the comparison of what the Plan actually earned on the [attacked] investment, with what the Plan would have earned had the fund been available for other Plan purposes. If the latter amount is greater than the former, the loss is the difference between the two; if the former is greater, no loss was sustained.

Donovan v. Bierwith, slip op. at 16.

This measure of opportunity cost is the appropriate measure of losses under Sec. 1109. While in *Donovan* there was only one purchase which had to be dealt with, the problems of loss determination in this case are exacerbated because there are three different transactions. Together the investments in the present case had a 72 per cent rate of return in about a year, a rate that was unlikely to be matched by other Plan investments. The Hickory purchases alone, however, netted only 4 per cent in about a year.

The court believes that though the decision to use the fund's assets for the purchases, and the strategy used, was determined as a whole, plaintiffs and intervenors may elect to seek to prove opportunity losses on some investment, presumably Hickory, while seeking restoration of profits on others.

B. Restoration of profits made through use of assets of the Plan.

In discussing the appropriate disgorgement remedy the Seventh Circuit stated that recovery of a fiduciary's profits could occur "only where there is a causal connection between the use of the Plan assets and the profits made by fiduciaries on the investment of their own assets." 727

F.2d at 137. "Plaintiff must be denied a windfall, but receive the benefit of such reasonable doubts as appear." *Id.* at 139. The court discussed certain copyright and trust cases where profits were apportioned according to what the profits were attributable. The court then stated that "the burden is on the defendants who are found to have breached their fiduciary duties to show which profits are attributable to their own investment, apart from their control of the Reliable Trust assets." *Id.* at 138.

This court received certain proposals by the parties and, dissatisfied, asked for new proposals. The second batch was not much different than the first. The intervening claimants have stated a generally proper standard:

> The Engle group must restore all profits and all benefits which each fiduciary admits was received as a result of investing Plan assets. "All profits and all benefits" must be defined for purposes of formulating the appropriate remedy to meet every advantage that could be measured in monetary terms at the close of the controller take-over fight initiated or maintained by the Engle group.

That does not, however, indicate how such advantages should be measured.

After much thought and in the absence of any alternative bases for measurement proposed by the parties which accord with the appellate mandate, despite two invitations to do so, the court has determined what basis it wishes to have followed in the disgorgement determinations. The court is concerned with the value to the Engle group of the trust's purchase of the shares in question. The value of something to a certain purchaser is equal to what the purchaser would be willing to pay for it. *See generally* R. Posner, *The Economics of Justice,* 60-61 (1981). There were two points in each of the Engle group's stock transactions where the trust's purchase of shares had value

to the Engle group: when they bought and when they sold. The court believes that the following determination is a proper method for transferring to the trust the value received by the Engle group through the trust purchases.

When the Engle group began to purchase the shares of the three corporations they undoubtedly endeavored to keep the fact of their purchases quiet as long as possible in order to keep the price of the shares down. Use of the trust assets to buy the shares of these companies may have allowed them to purchase their other shares at a lower price because of an absence of one identifiable group of purchasers. This advantage was noted by the Seventh Circuit when it stated that "the trust investments were made very early in the control contests, when it may have been particularly valuable to acquire the first shares discreetly." *Leigh v. Engle*, 727 F.2d at 138. Any price advantage to the trust was reflected in its purchase price and realized upon sale. Any price advantage received by the Engle group in their purchases of the Hickory, Berkely, and OSI stock, apart from the Plan and due to the Plan not being identified as a related purchaser, is, however, a profit attributable to the Plan investment. Thus, the difference between what was actually paid for the block of shares purchased by the Engle group other than the trust purchases, and what would have been paid for those shares if all shares, including the trust investment, had been purchased entirely by defendants, should be divested. It is expected that expert testimony will be required to determine the difference between the two prices, if any difference exists at all.

When the defendants sold the shares of Berkeley and OSI it can be presumed that the premium received was, in some part, due to the extent of their holdings in the company. For example, when the OSI shares were sold, the Engle group owned 21.73 per cent of the company. *See Leigh v. Engle*, 727 F.2d at 121. In negotiating a sale, the

Engle group was presumably able to negotiate a higher price than a group with 15 per cent, 10 per cent or 5 per cent. Of the block controlled by the Engle group, 1.22 per cent of the OSI stock was purchased by the trust assets. Any premium on the trust shares was realized upon sale. The trust fund is, however, intitled to recover whatever premiums there may have been on the Engle group shares other than the trust investment. That portion of any premium received on the other share because of that extra 1.22 per cent is attributable to use of the trust assets and is recoverable by the Plan. Finally, given the burden of proof upon defendants, it will be presumed that all profits are attributable to the Plan assets in the absence of evidence to the contrary.

As for the Hickory stock, where no resale by the Engle group occurred, any profit in excess of that realized may be determined by a valuation of the company. The Engle group picked Hickory as a target because it believed it to be undervalued. *See Leigh v. Engle*, 727 F.2d at 117. It may well be, therefore, that an objective valuation of the company at that time of purchase from the Plan would have valued it at more than the amount the Engle group paid for the stock. The trust purchased about one per cent of the company (12,000 shares). *See id.* at 122. The trust, therefore, deserves one per cent of the difference between the value of the company as of March 19, 1979, th date the trust sold its shares to defendants and the sales price to the Engle group. Again, expert testimony will probably be required to determine those values. Plaintiffs would probably be entitled to this amount or the difference between the opportunity value of the invested fund assets and the actual four per cent return, whichever is greater.

By requiring disgorgement of benefits obtained by both the purchase of the shares and the sale of the shares the court believes it most adequately restores to the Plan any profits of defendants "which have been made through use

of assets of the Plan by the fiduciary." *See* 29 U.S.C. § 1109 (a). The court recognizes that defendants are being required to disgorge benefits achieved at purchase, based on the assumption that they would have purchased the trusts' shares if the trust had not. This contradiction is warranted, however, by the heavy burden of proof that is place squarely upon defendants. *See Donovan v. Bierwith, supra,* slip op. at 17. The Seventh Circuit, in remanding this case, drew analogies with copyright law and explicitly approved a formulation requiring that "doubts shall be resolved against the defendants so that the amount awarded 'will favor the plaintiffs in every reasonable chance of error.' " *Leigh v. Engle, supra,* 727 F.2d at 138, *quoting Sheldon v. Metro-Goldwyn Pictures Corp.,* 106 F.2d 45, 51 (2d Cir. 1939) (Learned Hand, J.), *aff'd* 309 U.S. 390 (1940). The court also recognizes that the proof will be difficult in these areas. Again, the burden rests on defendants and doubts will be resolved against them, but only within the parameters outlined by the court.

III. Matters Still to be Litigated

Two issues of liability remain. First, the court must determine, in accordance with the principles laid out by the Seventh Circuit, *See Leigh v. Engle,* 727 F.2d at 132-36, whether Engle and Libco are liable as co-fiduciaries under 29 U.S.C. §§ 1104 and 1105. The court must also determine whether the defendants, or any of them, violated their fiduciary duties by delaying distribution of the trust. *See Leigh v. Engle,* 727 F.2d at 136-37. Finally, the court must determine what damages, if any, resulted from any improper delay. Evidence respecting investment and delay damages should be heard in the liability proceeding. Reimbursement issues, as well as sec. 1132(g) (1) attorneys' fees issues, will be subsequently determined. The court directs that the parties submit memoranda indicating what discovery, if any, each believes is necessitated by this Memorandum and Order and suggesting a schedule for

the final resolution of this litigation. Those submissions shall be filed by July 10, 1985. A Rule 16 conference is hereby scheduled for July 12, 1985 at 4:30 p.m.

/s/ JAMES B. MORAN
JAMES B. MORAN
Judge, United States District Court

June 27, 1985

United States District Court

For the Seventh Circuit

Chicago , Illinois 60604

May 30 , 1985 .

Before

Hon. RICHARD D. CUDAHY, Circuit Judge

Hon. _____

Hon. _____

CHARLES W. LEIGH and ERVIN F. DUSEK, etc.
Plaintiffs-Appellants,

GEORGE JOHNSON, et al.,
Intervening Plaintiffs-Appellants,

NOS. 82-2943, 82-3040 *VS.*

CLYDE WILLIAM ENGLE, et al.,
Defendants-Appellees.

Appeals from the United States District Court for the Northern District of Illinois, Eastern Division

No. 78 C 3799

Judge
George N. Leighton

This matter comes before the court for its consideration of the following documents:

1. "MOTION TO RECALL MANDATE AND FOR OTHER RELIEF" filed herein on May 6, 1985, by counsel for the interviening plaintiffs-appellants.

2. "PLAINTIFFS' RESPONSE TO INTERVENORS' MOTION TO RECALL MANDATE OR FOR

OTHER RELIEF" filed herein on May 16, 1985, by counsel for the plaintiffs-appellants.

3. "DEFENDANTS' MEMORANDUM IN OPPOSITION TO INTERVENORS' MOTION TO RECALL MANDATE AND FOR OTHER RELIEF" filed herein on May 13, 1985, by counsel for the defendants-appellees.

Plaintiffs have filed a motion to recall mandate contending that our mandate is sufficiently ambiguous as to require out intervention in the ongoing remand before Judge Moran. We find no such ambiguity in the opinion as to want clarification. Accordingly,

IT IS ORDERED that the motion to recall mandate and for other relief in DENIED.

Appeals 82-2943 and 82-3040

Plaintiffs also allege various improprieties regarding the manner in which the district court is handling the remand of this case. Our sole authority to influence the manner in which a district court is handling a case would be through our mandamus jurisdiction. Any contention with regard to Judge Moran's handling of this case might be better addressed in a Petition for Mandamus.

In the

United States Court of Appeals

For the Seventh Circuit

Nos. 82-2943 and 82-3040

CHARLES W. LEIGH and ERVIN F. DUSEK, etc.,

Plaintiffs-Appellants,

and

GEORGE JOHNSON, et al.,

Intervening Plaintiffs-Appellants,

v.

CLYDE WILLIAM ENGLE, et al.,

Defendants-Appellees.

Appeals from the United States District Court for the Northern District of Illinois, Eastern Division.
No. 78 C 3799—**George N. Leighton**, *Judge.*

ARGUED JUNE 6, 1983—DECIDED JANUARY 27, 1984

Before WOOD and CUDAHY, *Circuit Judges*, and GRANT, *Senior District Judge.**

CUDAHY, *Circuit Judge.* Plaintiffs in this case are beneficiaries of an employee benefit plan who alleged that the plan administrators and others had violated fiduciary

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* Honorable Robert A. Grant, Senior District Judge for the Northern District of Indiana, is sitting by designation.

duty provisions of the Employee Retirement Income Security Act of 1974, 29 U.S.C. §§ 1001—1461 ("ERISA"). The heart of the case is a dispute over how ERISA governs the actions of plan administrators and other fiduciaries with respect to investment activities in contests for corporate control. The beneficiaries allege that the plan administrators and other defendants violated ERISA when they used plan assets to purchase stocks of companies that were targets of the defendants' investment program. After a bench trial, the district court entered judgment for the defendants. We vacate and remand.

I.

Plaintiffs-appellants are beneficiaries of the Reliable Manufacturing Corporation Employees Profit Sharing Trust ("Reliable Trust"). This action was originally filed by Charles W. Leigh and Ervin F. Dusek; they are beneficiaries of the Reliable Trust and former owners of the Reliable Manufacturing Corporation ("Reliable Manufacturing"). Intervening plaintiffs are a class of all other Reliable Trust beneficiaries who have fully vested rights in the trust.

The Reliable Trust was created by Reliable Manufacturing in 1968 as an employees' profit sharing trust; the trust administrators were appointed by the Reliable Manufacturing board of directors. The Reliable Trust is subject to ERISA, and plaintiffs allege that the defendants-appellees violated their fiduciary duties under ERISA in a series of investments the Reliable Trust made in the spring of 1978. Until March 1978, the trust held all of its assets in the form of fixed income money market investments. In late March 1978, the trust invested approximately 30% of its assets in the stock of three companies: Berkeley Bio Medical, Inc. ("Berkeley"), Outdoor Sports Industries, Inc. ("OSI"), and the Hickory Furniture Company ("Hickory"). Both before and after the trust's purchases, other defendants made sizable investments in the same companies. Plaintiffs allege that

the investment of approximately 30% of the Reliable Trust's assets in these three companies was done to aid the defendants who hoped either to win control of the companies or to earn substantial "control premiums."

Defendants-appellees are a group of individuals and business entities with close connections to defendant Clyde W. Engle. The complex network of legal and financial relationships among the defendants is central to our disposition of this case, so we must trace them in some detail. Although defendants dispute the characterization, we will on occasion refer to them as the "Engle group."

A.

Clyde Engle stands at the center of the network. He is an Illinois financier and investor with numerous business interests.[1] Since 1976 Engle has been chairman of defendant Libco Corporation. In the spring of 1978, Engle owned 31.5% of Libco shares and through trusts for his children controlled an additional 6.4% of Libco. Supplemental Appendix at 496. He also had some degree of control over an additional 12% of Libco shares owned by the Sierra Capital Group, described below. Clyde Engle's offices are at Suite 1600, 625 North Michigan Avenue, Chicago, Illinois.

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[1] Other business activities of Engle and other defendants are described in several reported federal decisions. *See, e.g., Telvest, Inc. v. Bradshaw*, 697 F.2d 576 (4th Cir. 1983); *Issen v. GSC Enterprises, Inc.*, 508 F. Supp. 1278 (N.D. Ill. 1981); *Telvest, Inc. v. Wisconsin Real Estate Investment Trust*, 489 F. Supp. 250 (E.D. Wis. 1980); *Securities and Exchange Comm'n v. GSC Enterprises, Inc.*, 469 F. Supp. 907 (N.D. Ill. 1979). The investments in this case have also spawned other litigation. *See, e.g., Outdoor Sports Industries, Inc. v. Telvest, Inc.*, 88 F.R.D. 44 (N.D. Ill. 1980); *Libco Corp. v. Adams*, 100 Ill. App. 3d 314, 55 Ill. Dec. 805, 426 N.E.2d 1130 (1981) (defamation suit against plaintiffs' attorney in this case).

Defendant Libco Corporation is a holding company which purchased 100% of the common stock of Reliable Manufacturing from plaintiffs Leigh and Dusek in April 1977.[2] Libco also has offices at Suite 1600, 625 North Michigan Avenue in Chicago. In the spring of 1978, Libco owned 64% of the stock of defendant Telco Marketing Services, Inc. ("Telco"). At that time, Clyde Engle was chairman of the board, chief executive officer and treasurer of Telco. Telco's offices are also at Suite 1600, 625 North Michigan Avenue in Chicago.

Defendant Telvest, Inc. ("Telvest") is a wholly owned subsidiary of Telco formed on June 1, 1978, for investment purposes. Engle was president, treasurer and a director of Telvest in 1978. Telvest's offices are also located at Suite 1600, 625 North Michigan Avenue in Chicago.

Two other Engle businesses are not parties to this lawsuit, but their investments in Berkeley, OSI and Hickory in 1978 are relevant to the dispute here. First, GSC Enterprises, Inc. ("GSC") is a holding company which owns the Bank of Lincolnwood. In 1978 Engle was chairman of the board and president of GSC, as well as chairman of the board of the bank. GSC's offices are also located at Suite 1600, 625 North Michigan Avenue, Chicago. Second, the Sierra Capital Group ("Sierra") is an Illinois limited partnership engaged in investment activities. The general partner in Sierra is Sierra Associates, another Illinois limited partnership. Clyde Engle is one of two general partners of Sierra Associates. In the spring of 1978, among its other investments, Sierra owned 12% of Libco stock and 19% of GSC stock. Sierra's offices are also at Suite 1600, 625 North Michigan Avenue in Chicago.

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[2] Reliable Manufacturing went into involuntary bankruptcy proceedings in March 1979 and was declared bankrupt on December 6, 1979. The sale of Reliable Manufacturing and the subsequent bankruptcy proceedings are described in *In re Reliable Manufacturing Corp.*, 703 F.2d 996, 998-99 (7th Cir. 1983).

Defendant Nathaniel Dardick is an attorney who played key roles in all of the organizations described above. Dardick graduated from the University of Chicago Law School in 1974. He was associated for several years with the Chicago firm of Sachnoff Schrager Jones Weaver & Rubenstein, which did work for Clyde Engle.[3] He then established his own firm with offices at Suite 1600, 625 North North Michigan Avenue in Chicago. During 1978 and 1979, Dardick was retained as personal counsel to Clyde Engle. He was also general counsel to Libco, Telco, Telvest, GSC, the Bank of Lincolnwood and Sierra. The record does not show clearly whether Dardick had other clients in 1978 and 1979, but it is clear that Engle and these organizations accounted for most of Dardick's income from his law practice.[4] Dardick is also one of two administrators of the Reliable Trust, and he had direct control over the trust's investments in 1978 and 1979.

Defendant Ronald Zuckerman was president of Reliable Manufacturing and a member of the Reliable Manufacturing board of directors in 1977 and 1978. However, he received no salary from Reliable Manufacturing. He was paid only as a member of the Libco board and as an investment consultant to Libco. Zuckerman was also the other administrator of the Reliable Trust. He and Dardick were appointed administrators in September 1977 by the Reliable Manufacturing board of directors, composed of Engle, George Contarsy and Zuckerman himself. (Engle, Contarsy and Zuckerman were also directors of Libco.) Neither Dardick nor Zuckerman received compensation as trust administrators. Zuckerman's offices are also at Suite 1600, 625 North Michigan Avenue in Chicago.

Charles Newbill was originally named as a defendant in the case, but he was never served with the complaint. His

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[3] The firm of Sachnoff Weaver & Rubenstein has represented all defendants in this lawsuit at trial and on appeal.

[4] *See* Supplemental Appendix at 294-304.

role in the case is central, for he was the investment analyst who identified the investment opportunities for Dardick and the Reliable Trust, as well as for Engle, Libco, Telco, Telvest, Sierra and GSC. Newbill first met Engle when both worked at the Harris Bank in Chicago. Newbill was also a general partner in Sierra Associates between 1970 and 1972, and he worked abroad briefly. Newbill went to work for Libco and Engle as an investment consultant in 1976. During 1977 and part of 1978, Libco was Newbill's only paying client.[5] According to Newbill's testimony, he sought financial information from several thousand companies, analyzed their replies to look for undervalued companies, and identified thirty companies which he thought had good investment potential for Libco. During the early months of 1978, Newbill talked with both Engle and Dardick about his research, and he narrowed the list of investment targets. To both Engle and Dardick, he recommended investments in Berkeley Bio Medical, Inc. ("Berkeley"), Hickory Furniture Company ("Hickory"), and Outdoor Sports Industries, Inc. ("OSI"). Newbill's office was also at Suite 1600, 625 North Michigan Avenue in Chicago.

Defendant National Boulevard Bank is now trustee of the Reliable Trust. The bank became trustee on February 5, 1979, after the challenged investments were made but while the trust still held its shares of OSI and Hickory. The bank is a defendant because all plaintiffs seek an immediate distribution of the assets remaining in the trust.

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[5] Newbill submitted a bill to the Reliable Trust for investment advice given in early 1978, but the bill was not prepared until December 1978, several months after this litigation was filed to challenge the investments Newbill recommended. To the extent that Newbill provided investment counseling to the Reliable Trust, he may be considered a fiduciary of the trust. *See* 29 U.S.C. § 1002(21)(A)(ii).

B.

Plaintiffs' claim here depends upon the relationships between the Reliable Trust's investments in Berkeley, OSI and Hickory, and the activities of other members of the Engle group. Therefore we must examine the activities in considerable detail.

The Engle group's investment and acquisition plans for Berkeley, Hickory and OSI appear in the records of a meeting of the Telco board of directors on April 21, 1978. Supplemental Appendix at 424-29. The meeting was held at Suite 1600, 625 North Michigan Avenue in Chicago. Engle chaired the meeting and Dardick acted as secretary.[6] Engle informed the board that Telco had approximately $2,000,000 available for investment, and he recommended that Telco invest the money in up to 10% of the outstanding shares of Berkeley, Hickory and OSI. Newbill presented to the board his analysis of the three companies. The minutes of the meeting show that the Telco board learned that members of the group had already begun to establish positions in each of the three companies:

> As part of these discussions, the Board was also advised of the ownership positions in such companies of certain affiliates of the Company and associates of certain directors of the Company, namely Libco Corporation, GSC Enterprises, Inc., Clyde Wm. Engle, Sierra Capital Group, Ronald K. Zuckerman *and the Reliable Manufacturing Corporation Employees' Profit Sharing Trust.* In particular, it was disclosed that the following persons own shares of Berkeley, Hickory and OSI in the amounts set opposite their respective names as follows:

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[6] Zuckerman did not attend the meeting.

	Berkeley	Hickory	OSI
Libco Corporation		47,000	
Clyde Wm. Engle	41,670		3,500
GSC Enterprises, Inc.	32,100	4,000	8,000
Ronald K. Zuckerman	1,200		
Sierra Capital Group	21,600		
Reliable Profit-Sharing Trust	*15,000*	*8,000*	*12,500*

Supplemental Appendix at 426 (emphasis supplied). At the time of the April 21st meeting, the various members of the Engle group, including Telco,[7] owned approximately 5.58% of outstanding Berkeley shares, 2.98% of outstanding OSI shares and 4.88% of outstanding Hickory shares. Short Appendix at 29-33. The Telco board adopted a resolution authorizing management to purchase approximately 10% of the outstanding shares of the three companies, but the resolution also put ceiling prices on the purchases. The resolution authorized Telco to consolidate the group's holdings by purchasing shares owned by Sierra, Engle, Libco and GSC. Supplemental Appendix at 427. After the April 21st meeting, virtually all of the group's further purchases of the three stocks were made by Telco or by its subsidiary, Telvest, formed in June 1978.

Thus, during 1978 when the Reliable Trust invested 30% of its assets in Berkeley, OSI and Hickory, other members of the Engle group were purchasing substantial amounts of stock in the three companies both before and after the trust purchases.[8] Plaintiffs contend that the Engle group purchases and the trust's purchases were

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[7] Telco began to purchase Berkeley and OSI shares on April 17, 1978.

[8] The appellants have not pressed in this court their claims regarding trust investments in other securities, including Bank of Lincolnwood capital notes and Joseph Dixon Crucible Company common stock. Therefore, we have not considered the district court's findings with respect to those investments.

part of a concerted investment and acquisition program by Engle and his associates. They allege that the trust's assets were invested to enhance the Engle group's position with respect to control of the three target companies.

There is no claim here that the Reliable Trust lost any money through the disputed investments. Indeed, the trust profited handsomely from its investments in Berkeley and OSI.[9] Instead, plaintiffs here claim that the trust's assets were put at risk to benefit the Engle group in its program of acquisitions.[10]

1. *Berkeley investments*: The Engle group's interest in Berkeley began in early 1978, when Berkeley was the target of an unfriendly takeover attempt by Cooper Laboratories, Inc. ("Cooper"). Berkeley president Irving Abramowitz asked Engle to help him defend against the takeover, and Engle purchased more than 60,000 shares of Berkeley stock for himself and GSC in January 1978.

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[9] The Reliable Trust's investments in Berkeley, OSI and Hickory may be summarized as follows:

	Number of Shares	Purchase Price	Sale Price	Profits	Return on Investment
Berkeley	15,800	$ 71,580.53	$118,500.00	$ 46,919.47	66%
OSI	12,500	77,736.83	187,500.00	109,763.17	141%
Hickory	12,000	72,433.21	75,000.00	2,566.79	4%
Totals		$221,750.57	$381,000.00	$159,249.43	72%

Profits and return on investment do not include dividends received.

[10] It is not clear whether the Engle group intended to acquire majority control of Berkeley, OSI or Hickory. The group eventually acquired a majority of Hickory stock, but Hickory management did not oppose the acquisition. Both Berkeley and OSI management resisted the Engle group's acquisition efforts, and the Engle group succeeded in acquiring only 10.7% and 22% of the two companies respectively. The Reliable Trust made substantial profits on its Berkeley and OSI investments, yet made very little profit on the Hickory investments. *See supra* note 9.

By the beginning of March, Sierra and Zuckerman had also purchased Berkeley shares, and the holdings of Engle, GSC, Sierra and Zuckerman amounted to approximately 3.6% of Berkeley shares.

In late February, Engle learned that Abramowitz and Cooper were planning a deal to settle their control contest. Berkeley management planned to give Cooper control of Berkeley's medical equipment subsidiary in return for Cooper's shares of Berkeley. The deal would have kept Abramowitz in control of Berkeley. Engle thought the proposed deal would be disadvantageous to minority shareholders such as himself. Supplemental Appendix at 554-61. Plaintiffs contend that Engle was "locked in" as a minority shareholder under hostile management, and that he sought to escape his position by increasing his control of the company. Engle bought an additional 11,200 shares of Berkeley for himself and GSC between February 27th and March 10th.

Between March 17, 1978, and March 31, 1978, the Reliable Trust bought at Dardick's direction 15,800 shares of Berkeley stock at a total cost of $71,580.53. Those 15,800 shares represented approximately 10% of the trust's assets at the time and constituted 0.65% of the outstanding Berkeley shares. Adding the trust's shares to those owned by Engle, Zuckerman, GSC and Sierra, the group owned a total of 4.65% of Berkeley at the end of March 1978.

While the Reliable Trust was buying Berkeley shares on his orders, Dardick was helping Engle respond to the proposed deal between Berkeley and Cooper. On March 22, 1978, Engle sent letters on GSC letterhead to the Berkeley outside directors protesting the proposed deal and arguing that it was contrary to the interests of minority shareholders. He described the transaction as an "improper sweetheart deal." The letters suggested that Engle would take further steps if necessary to protect the interests of minority shareholders. Dardick helped Engle prepare these letters and actually signed Engle's name to

them. About two weeks later, Engle, Sierra and GSC filed suit to enjoin consummation of the deal between Berkeley and Cooper.[11] Dardick acted as their attorney in the suit. Thus, at the same time Dardick was investing 10% of the Reliable Trust's assets in Berkeley stock, he and Engle were arguing that Berkeley management was acting contrary to the interests of minority shareholders such as the Reliable Trust.

In April Telco began to purchase Berkeley shares, and by August the Engle group owned 10.72% of Berkeley stock. The litigation initiated by Engle and his associates to enjoin the Berkeley-Cooper deal was settled in August 1978 by having Cooper buy the Berkeley shares controlled by the Engle group for a very profitable price. The Reliable Trust was not a party to the lawsuit, nor were trust funds used in the litigation. However, the trust's shares were included in the settlement.[12]

2. *OSI investments*: In March 1978, the Reliable Trust and GSC began purchasing OSI stock. By the end of March, the trust owned 12,400 shares and GSC owned 5,100 shares, totalling 1.22% of the outstanding OSI shares. The trust had spent $77,736.83 for its shares of OSI. At the time of the April 21st Telco board meeting, GSC, Engle, Telco and the Reliable Trust owned 42,800

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[11] Telco, Libco, Engle and Sierra filed a Schedule 13D with the Securities and Exchange Commission in April 1978 regarding their purchases of Berkeley stock. In the list of Berkeley shares held by the reporting persons and their associates, the Reliable Trust shares of Berkeley were included. Their inclusion in the list is by no means conclusive as to whether the trust shares were "used by" the Engle group. However, the inclusion of the Reliable Trust's holdings in the SEC filing is clear evidence that the reporting persons—Engle, Libco, Telco and Sierra—knew of the trust's Berkeley investments.

[12] Defendants apparently contend that this inclusion of the Reliable Trust shares in the settlement was a generous act to benefit the trust. Brief of Defendants at 37.

shares of OSI, or approximately 2.98% of the outstanding shares. Telco and later Telvest continued to purchase OSI stock steadily until March 1979, when the group's holdings were 312,400 shares, or 21.73% of outstanding shares. On May 3, 1978, Engle and Newbill visited OSI management and asked that Engle be put on the OSI board, but the proposal was rejected. A few days later, Telco and Libco filed with the Securities and Exchange Commission a Schedule 13D revealing the Engle group's purchases of OSI stock and their intentions to acquire more shares. The Schedule 13D said "Libco may be deemed to own beneficially an additional 12,500 shares of OSI owned of record by the Reliable Manufacturing Corporation Employees Profit Sharing Trust ('Reliable Trust')," and it stated that Libco could elect the directors of Reliable who in turn appointed the Reliable Trust administrators. The statement also noted that Zuckerman was a director of both Libco and Reliable, president of Reliable and one of the Reliable Trust administrators. In the Schedule 13D, Libco expressly disclaimed "any beneficial interest in the assets of the Reliable Trust."[13]

In early 1979 the Engle group battled OSI management for control of the company through two tender offers and a proxy fight. Documents filed in the tender offers continued to show the relationship between the Reliable Trust and other group members. Dardick acted as attorney for Telco in the tender offers and for Telvest in the proxy fight. During the proxy fight, Dardick ordered the Harris Bank as trustee to vote the trust's shares in favor of the Telvest slate of directors on April 24, 1979. During these struggles, Dardick was sharply critical of OSI management and the company's profitability. At the same time,

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[13] Neither the mention of the trust's shares nor the disclaimer is conclusive regarding the use of the trust's assets. However, the filing is clear evidence that Libco, Telco and Engle (who signed the filing for Telco) knew of the trust's investments in OSI. *See supra* note 11.

Dardick controlled the Reliable Trust's investments in OSI, and his statements indicate that he believed the investments could have turned out well only if OSI management could have been replaced, or if the trust could have sold its shares to a "white knight" for a premium.

By May 1979, the Engle group controlled 21.73% of OSI shares. The control contest ended when the Brown Group, Inc., entered as a "white knight" on behalf of OSI management and tendered $15.00 per share of OSI stock. On June 26, 1979, the Reliable Trust sold its OSI shares to the Brown Group for a profit of 141%.

3. *Hickory Furniture investments*: Hickory was the third investment target, and the Engle group succeeded in purchasing a majority of Hickory stock by October 1979. The Reliable Trust bought 8000 shares of Hickory on March 22, 1978. At that time, Libco and GSC already owned 50,400 shares, and the trust purchases gave the group 4.88% of outstanding Hickory stock. After the April 21st Telco meeting, Telco and later Telvest steadily acquired Hickory stock.[14] The Reliable Trust purchased an additional 4000 shares of Hickory on June 9, 1978. Hickory management did not resist the Engle group investments, and on June 28th, Engle became a member of the Hickory board of directors. By the end of 1978, the Engle group owned 32.8% of Hickory, and their holdings grew to 52.8% in October 1979. The Reliable Trust sold its

[14] Libco and Telco filed a Schedule 13D with the Securities and Exchange Commission in May 1978 regarding their purchases of Hickory stock. Later filings to update the original Schedule 13D describe the Reliable Trust's holdings of Hickory stock and say that "Libco may be deemed to own beneficially" the trust's shares. Libco also disclaimed "any beneficial interest in the assets of the Reliable Trust." Again, the statements in the SEC filings are not conclusive as to whether the Engle group used the Reliable Trust's assets in its acquisition program. *See supra* notes 11 and 13. Nevertheless, the filings cleary show that Telco, Libco and Engle were aware of the Reliable Trust's Hickory investments.

12,000 shares of Hickory on March 19, 1979, one year after its initial purchase, for a net profit of 4%.

C.

The case before us was tried in the district court before Judge Leighton in September 1982. The district court granted judgment for defendants in an unpublished memorandum issued November 18, 1982. The district court held first that ERISA does not create a cause of action where the plan does not suffer financial loss. Conclusion of Law No. 10. The district court also found that the defendants did not use the Reliable Trust assets for their own purposes and that the assets were used exclusively in the interest of the trust beneficiaries. Findings of Fact Nos. 11, 12, 13 and 18; Conclusions of Law Nos. 4 and 15. The district court held that Dardick, Zuckerman and the National Boulevard Bank were fiduciaries of the trust, but that they had not violated their duties under ERISA sections 404 and 406, 29 U.S.C. §§ 1104 and 1106, by investing the trust assets in Berkeley, OSI and Hickory. Conclusions of Law Nos. 2, 4, 5, 6 and 15. The court concluded that the plan assets had been used for the exclusive benefit of the plan beneficiaries, Conclusion of Law No. 15, and that the plan administrators acted in good faith, Finding of Fact No. 23. The court also concluded that Dardick, Zuckerman and the National Boulevard Bank did not breach their co-fiduciary obligations under 29 U.S.C. § 1105(a). The court held further that Engle, Libco, Telco and Telvest had not exercised discretionary authority over the Reliable Trust and were not fiduciaries with respect to the investment or administration of its assets. Findings of Fact Nos. 21 and 22; Conclusion of Law No. 7. The court awarded expenses and attorneys' fees to all defendants and held that Dardick, Zuckerman and the National Boulevard Bank were entitled to reimbursement of expenses and fees from the trust's remaining assets. Conclusion of Law No. 16.

II.

The Reliable Trust's investments in Berkeley, OSI and Hickory produced in the aggregate the extraordinary return on investment of 72%, exclusive of dividends.[15] It is clear that the trust lost no money in the challenged transactions. The district court held that ERISA creates no cause of action where a breach of fiduciary duty does not cause financial harm to the benefit plan, Conclusion of Law No. 10, but the district court erred in this statement of the law. ERISA clearly contemplates actions against fiduciaries who profit by using trust assets, even where the plan beneficiaries do not suffer direct financial loss.[16] A fiduciary who breaches his duties "shall be personally liable . . . to restore to such plan any profits of such fiduciary which have been made through use of assets of the plan by the fiduciary." 29 U.S.C. § 1109(a).

The nature of the breach of fiduciary duty alleged here is not the *loss* of plan assets but instead the *risking* of the trust's assets at least in part to aid the defendants in their acquisition program. ERISA expressly prohibits the use

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[15] See *supra* note 9.

[16] The district court's reliance on *Alton Memorial Hospital v. Metropolitan Life Ins. Co.*, 656 F.2d 245, 249 (7th Cir. 1981), is misplaced. That case involved a contractual dispute between an employer who maintained a pension plan and the enrolled actuary of the plan. This court there held that the actuary could not invoke ERISA's fiduciary standards to recover from the employer in the contractual dispute between them. It was clear that the interests of the plan beneficiaries were not affected in any way, and thus ERISA did not create a cause of action on behalf of the actuary. In the present case, by contrast, the interests of plan beneficiaries were directly affected. The defendants appear to have risked the trust assets in part to serve their own purposes rather than solely the interests of the beneficiaries. With its focus on protecting the interests of plan beneficiaries, ERISA clearly prohibits such actions, and the provisions in section 1109(a) for disgorgement of profits are the remedy to deter such violations.

of assets for purposes other than the best interests of the beneficiaries, and the language of section 1109(a) providing for disgorgement of profits from improper use of trust assets is the appropriate remedy.[17] On the record before us, we are unable to determine the extent of the defendants' total profits, and we certainly cannot measure the extent, if any, to which any profits resulted from the defendants' use of the trust assets. However, those questions are relevant only in measuring damages. *See infra* Part VI. At this point in the analysis, we need only say that plaintiffs are not required to show that the trust lost money as a result of the alleged breaches of fiduciary duties. If ERISA fiduciaries breach their duties by risking trust assets for their own purposes, beneficiaries may recover the fiduciaries' profits made by misuse of the plan's assets.

III.

ERISA requires those who control employee benefit plans to act solely in the interests of the plan beneficiaries. The fiduciary duties of those who control benefit plans are set forth in part 4 of Title I of ERISA. Two sections are applicable to this case. First, section 404(a), 29 U.S.C. § 1104(a), codifies and makes ap-

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[17] The legislative history of ERISA shows that Congress intended disgorgement of profits to be one remedy available for breach of fiduciary duty. A fiduciary who breaches this duty "must restore to the plan any profits which he made using plan assets." S. REP. NO. 383, 93rd Cong., 1st Sess. 105, *reprinted in* 1974 U.S. CODE CONG. & AD. NEWS 4890, 4988. The disgorgement provisions of § 1109(a) are in accord with the common law of trusts. *See* RESTATEMENT (SECOND) OF TRUSTS § 205(b), comment (h), and § 206 comment (j) (1959). *See also Home Federal Savings & Loan Ass'n v. Zarkin*, 89 Ill. 2d 232, 59 Ill. Dec. 897, 432 N.E.2d 841, 848 (1982). The purpose of this strict rule is to deter breaches by denying fiduciaries any profits from their misuse of assets. G. BOGERT, THE LAW OF TRUSTS AND TRUSTEES § 543 at 218 (rev. 2d ed. 1978).

plicable to fiduciaries[18] certain principles developed in the law of trusts.[19] H.R. REP. NO. 533, 93rd Cong., 1st Sess. 11, 13, *reprinted in* 1974 U.S. CODE CONG. & AD. NEWS 4639, 4649, 4651. Section 404(a)(1) provides in relevant part that:

> a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and—
>
> (A) for the exclusive purpose of:
>
> (i) providing benefits to participants and their beneficiaries; and

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[18] "Fiduciary" is defined in ERISA as follows:

> (A) Except as otherwise provided in subparagraph (B), a person is a fiduciary with respect to a plan to the extent (i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets, (ii) he renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan. Such term includes any person designated under section 1105(c)(1)(B) of this title.

29 U.S.C. § 1002(21)(A). We discuss below the application of this definition to the defendants in this case.

[19] As one district court has stated:

> The legislative history of the [fiduciary duty] sections of ERISA indicates, that to the extent practical, the obligations of trustees of pension funds and the limitations on their power of investment were to be interpreted under principles applicable to trustees under the common law of trusts, with a view toward establishing uniform standards.

Marshall v. Teamsters Local 282 Pension Trust Fund, 458 F. Supp. 986, 990 (E.D.N.Y. 1978) (fn. omitted).

> (ii) defraying reasonable expenses of administering the plan;
>
> (B) with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims . . . .

29 U.S.C. § 1104(a)(1). For the case before us, the key provisions are those requiring the fiduciary to act "solely in the interest" of plan beneficiaries and for "the exclusive purpose" of providing benefits. Other federal courts have described the duty of loyalty under ERISA as the duty to act with "complete and undivided loyalty to the beneficiaries of the trust," *Freund v. Marshall & Ilsley Bank*, 485 F. Supp. 629, 639 (W.D. Wis. 1979), and with an "eye single to the interests of the participants and beneficiaries," *Donovan v. Bierwirth*, 680 F.2d 263, 271 (2d Cir.), *cert. denied*, 103 S. Ct. 488 (1982).

Second, section 406 of ERISA, 29 U.S.C. § 1106, prohibits transactions in which the potential for misuse of plan assets is particularly great. The prohibited transaction rules focus primarily on the relationship between the benefit plan and other parties to a transaction, and the section prohibits transactions where those dealing with the plan may have conflicting interests which could lead to self-dealing. For example, section 406(a)(1)(B) prohibits loans between benefit plans and parties in interest. The *per se* rules of section 406 make much simpler the enforcement of ERISA's more general fiduciary obligations. *See* S. REP. NO. 383, 93rd Cong., lst Sess. 95, *reprinted in* 1974 U.S. CODE CONG. & AD. NEWS 4890, 4979.

Section 406 also includes broader language which may require a more detailed analysis of the fiduciary's actions. The provisions relevant to this case are:

> (a) Except as provided in section 1108 of this title:
>
> (1) A fiduciary with respect to a plan shall not cause the plan to engage in a transaction, if he

> knows or should know that such transaction constitutes a direct or indirect—
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> * * *
>
> (D) transfer to, or use by or for the benefit of, a party in interest, of any assets of the plan . . . .
>
> * * *
>
> (b) A fiduciary with respect to a plan shall not—
>
> (1) deal with the assets of the plan in his own interest or for his own account . . . .

29 U.S.C. § 1106. The relevant language here is quite broad: "use by or for the benefit of, a party in interest," § 1106(a)(1)(D),[20] and "deal . . . in his own interest," § 1106(b)(1).

The district court found that Dardick and Zuckerman did not breach their fiduciary duties under ERISA by purchasing and holding stock in Berkeley, OSI and Hickory. The court found that the purchases were made upon the advice of Newbill and were intended to diversify the plan's investments. The court also held that it was not improper for the Reliable Trust to hold its stock in Berkeley, OSI and Hickory after Telco made major purchases of the stocks. The court concluded that the trust's investments were prudent and made exclusively for the benefit of the trust beneficiaries. The court also found that the purchases were not prohibited transactions under section 406. The district court therefore concluded that Dardick and Zuckerman did not breach their fiduciary duties under section 404 and section 406.

We must accept the district court's findings of fact unless we find them "clearly erroneous." FED. R. CIV. P.

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[20] ERISA defines "party in interest" at 29 U.S.C. § 1002(14). The definition includes Reliable Manufacturing, Libco, Telco, Telvest, Engle, Zuckerman, Dardick and the National Boulevard Bank. 29 U.S.C. § 1002(14)(A), (B), (C), (E), (G) and (H).

52(a); *Clark v. Universal Builders, Inc.*, 706 F.2d 204, 206 (7th Cir. 1983). In this case, however, many of the district court's most important "Findings of Fact" regarding the use of the trust's assets are mixed findings of fact and law. *See* Findings of Fact Nos. 11, 12, 13, 17, 18, 19, 21, 22. Our review of these findings is consequently less deferential than it might otherwise be. *Harrison v. Indiana Auto Shredders Co.*, 528 F.2d 1107, 1120 (7th Cir. 1975). *See Lektro-Vend Corp. v. Vendo Co.*, 660 F.2d 255, 262-63 (7th Cir. 1981) (review of mixed findings and "paper" cases), *cert. denied*, 455 U.S. 921 (1982). Further, the evidence relevant to our conclusions on the critical issues in this case consists of documents and undisputed oral testimony. The district court's findings on issues where the observation of witnesses is critical are, of course, fully subject to the clearly erroneous rule. However, the district court's findings as to the defendants' credibility and good faith are not relevant to our disposition of this case, and thus we do not decide whether they were clearly erroneous. *See* Finding of Fact No. 23. This litigation concerns the legal significance of undisputed facts—the disputed issues of credibility and subjective good faith simply do not come into play. Good faith is not a defense to an ERISA fiduciary's breach of the duty of loyalty. *See Donovan v. Bierwirth*, 538 F. Supp. 463, 470 (E.D.N.Y. 1981), *aff'd as modified*, 680 F.2d 263 (2d Cir.), *cert. denied*, 103 S. Ct. 488 (1982).

In our view, application of ERISA's fiduciary standards to the Reliable Trust's investments in the corporate control contests here requires us to reverse the judgment below. The undisputed facts in the record show that the district court clearly erred when it concluded that plan assets were used exclusively in the interests of beneficiaries. The Reliable Trust administrators did not act solely in the interests of the plan beneficiaries where they invested the trust's assets in companies involved in corporate control contests, where the administrators themselves were actively engaged in the control contests and had substantial interests in them, where the admin-

istrators failed to make an intensive and independent investigation of the investment options open to the trust and where the trust's investment decisions never deviated from the best interests of the Engle group.

A. *Fiduciary Standards of Section 404.* The Second Circuit applied the fiduciary standards of section 404 to fiduciaries' conduct in a contest for corporate control in *Donovan v. Bierwirth*, 680 F.2d 263 (2d Cir.), *cert. denied*, 103 S. Ct. 488 (1982). At issue were the actions of Grumman Corporation's pension fund trustees during the Grumman-LTV takeover battle. The trustees were also Grumman officers. The district court had stated that Grumman corporate insiders with fiduciary duties to the corporation's pension fund would be tested against a standard requiring them to undertake a vigorous and independent investigation into the wisdom of the contemplated investment in order to meet the section 404(a)(1)(B) standards:

> [their] independent investigation into the basis for an investment decision which presents a potential conflict of interests must be both intensive and scrupulous and must be discharged with the greatest degree of care that could be expected under all the circumstances by reasonable beneficiaries and participants of the plan.

Donovan v. Bierwirth, 538 F. Supp. 463, 470 (E.D.N.Y. 1981), *aff'd as modified*, 680 F.2d 263 (2d Cir.), *cert. denied*, 103 S. Ct. 488 (1982).

Writing for the Second Circuit on appeal, Judge Friendly considered two approaches to analyzing the trustees' duty of loyalty in managing plan assets during the takeover battle. The first approach focused on the existence of conflicting interests between the trustees and the plan beneficiaries. The pension trustees were obliged to make their decisions, Judge Friendly wrote, "with an eye single to the interests of the participants and beneficiaries." 680 F.2d at 271. That duty of loyalty imposed upon the trustees a duty "to avoid placing them-

selves in a position where their acts as officers and directors of the corporation will prevent their functioning with the complete loyalty to participants demanded of them as trustees of a pension plan." *Id.*[21] Where the plan trustees were officers of the takeover target, and where they clearly had substantial career and financial interests in the outcome of the control contest, the court said it believed it would have been "almost impossible" for the trustees to have decided to use the trust assets in ways which would weaken their own position in the control contest, regardless of the interests of the plan beneficiaries. 680 F.2d at 272. Thus, the first approach the Second Circuit considered would require fiduciaries who face substantial conflicts of interest in corporate control contests to step aside so that a neutral trustee could act for the duration of the control contest. The court approved of this approach, 680 F.2d at 271-72, but chose to rest its decision instead on the second approach which examined in great detail the trustees' investigation of the alternatives open to them. The court held that the trustees' investigations did not amount to the thorough, careful and impartial investigation needed to justify actions which would, at least incidentally, benefit themselves and their corporation, apart from their effects on the beneficiaries of the trust:

> they should have realized that, since their judgment on this score could scarcely be unbiased, *at the least they were bound to take every feasible precaution to see that they had carefully considered the other side*, to free themselves, if indeed this was humanly possible, from any taint of the quick negative reaction

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[21] We recognize, as did the court in *Donovan v. Bierwirth*, that ERISA contains express exceptions which permit fiduciaries to act in a few limited situations where their interests and those of plan beneficiaries may diverge. *See* 29 U.S.C. § 1108. However, the exceptions of section 1108 are quite limited, and abuses are reasonably easy to detect where, for example, a trustee pays himself an excessive salary. None of the exceptions in section 1108 is applicable here.

> characteristic of targets of hostile tender offers . . . , and particularly to consider the huge risks attendant on purchasing additional Grumman shares at a price substantially elevated by the tender offer.

680 F.2d at 276 (emphasis supplied).

Under the section 404(a) duty of loyalty, the central question is whether the fiduciaries acted solely in the interests of the beneficiaries and for the exclusive purpose of providing them with benefits. The two approaches considered in *Donovan v. Bierwirth* offer two avenues for dealing with this central question. The first avenue focuses on the potential for conflicts of interest between the fiduciaries and the plan beneficiaries. Where the potential for conflicts is substantial, it may be virtually impossible for fiduciaries to discharge their duties with an "eye single" to the interests of the beneficiaries, and the fiduciaries may need to step aside, at least temporarily, from the management of assets where they face potentially conflicting interests. The second avenue involves a broader inquiry into the fiduciaries' actions where they may have substantial interests in a control contest. In *Donovan v. Bierwirth*, the Second Circuit focused on the fiduciaries' actions in investigating the investment options open to the plan during the corporate control contest. Where it might be possible to question the fiduciaries' loyalty, they are obliged at a minimum to engage in an intensive and scrupulous independent investigation of their options to insure that they act in the best interests of the plan beneficiaries. 538 F. Supp. at 470; 680 F.2d at 272. In the case before us, we believe there is an additional factor which weighs heavily in evaluating the loyalty of the fiduciaries. Here the control efforts lasted for several months, and in the case of Hickory, for over a year. The Reliable Trust held its shares involved in the control contests throughout these periods, and, as we discuss below, the trust's use of its assets at all relevant times tracked the best interests of the Engle group in the control contest. We believe that the extent and duration of these actions congruent with the interests of another party are

also relevant for courts in deciding whether plan fiduciaries were acting solely in the interests of plan beneficiaries.

B. *Prohibited Transactions Under Section 406.* Before discussing the application of the fiduciary standards to this case, we must also examine the applicability of the prohibited transaction provisions of section 406. In *Donovan v. Bierwirth*, the Second Circuit declined to apply the prohibited transaction provisions of section 406 to that case involving the use of an employee pension plan's assets to defend the employer from a hostile tender offer. 680 F.2d at 270. Specifically, the court there refused to apply the provisions of section 406(b)(2) prohibiting a fiduciary from acting on behalf of a party with interests adverse to the plan or its participants and beneficiaries. The Second Circuit stated that subsection (b)(2) was the only "arguably applicable" provision in section 406. The court said:

> We see no reason to think Congress intended the expansive interpretation of the various specific prohibitions of § 406 urged by the Secretary, particularly in light of the inclusion of the sweeping requirements of prudence and loyalty contained in § 404.

680 F.2d at 270.

However, we believe that the protective provisions of section 406(a)(1)(D) and (b)(1) should be read broadly in light of Congress' concern with the welfare of plan beneficiaries. We read those provisions dealing with the use of plan assets for the benefit of "parties in interest" and plan fiduciaries as a gloss on the duty of loyalty required by section 404.

We do not believe that Congress intended the language "use by or for the benefit of, a party in interest," § 406(a)(1)(D), and "deal . . . in his own interest," § 406(b)(1), to be interpreted narrowly. The entire statutory scheme of ERISA demonstrates Congress' overriding concern with the protection of plan beneficiaries, and we would be reluctant to construe narrowly any protective provisions of the Act.

The broad provisions of section 406(a)(1)(D) and (b)(1) require courts to look carefully at the transaction to decide whether plan assets were used "by or for the benefit of" a party in interest, or whether a fiduciary dealt with the plan assets "in his own interest." Application of these provisions may require courts to engage in the same searching investigation into the objective circumstances of the fiduciary's actions needed to apply the fiduciary loyalty provisions of section 404(a)(1).

Section 406(a)(1)(D) should be read to cover the actions of a trustee who buys shares in a target corporation in order to assist either the target's management or the raider in its quest for corporate control or a "control premium." If the corporation which the fiduciary seeks to aid qualifies as a "party in interest," we see nothing in the language or legislative history of subsection (a)(1)(D) which would preclude a court from treating the purchase as the use of plan assets for the benefit of a party in interest, at least where other evidence shows the fiduciary's purpose. *See Dimond v. Retirement Plan*, 4 EMPLOYEE BEN. CAS. (BNA) 1457, 1463 (W.D. Pa. Mar. 7, 1983) (enjoining use of plan assets to protect employer's incumbent management). The legislative analysis of subsection (a)(1)(D) clearly anticipates such an application of the subsection:

> [Subsection (a)(1)(D)] prohibits the direct or indirect transfer of any plan income or assets to or for the benefit of a party-in-interest. It also prohibits the use of plan income or assets by or for the benefit of any party-in-interest. As in other situations, *this prohibited transaction may occur even though there has not been a transfer of money or property between the plan and a party-in-interest. For example, securities purchases or sales by a plan to manipulate the price of the security to the advantage of a party-in-interest constitutes* [sic] *a use by or for the benefit of a party-in-interest of any assets of the plan.*

H.R. CONF. REP. NO. 1280, 93rd Cong., 2d Sess. 308, *reprinted in* 1974 U.S. CODE CONG. & AD. NEWS 5038, 5089 (emphasis supplied).

In addition, subsection (b)(1) could be applicable to an administrator's investment activities in the context of a corporate control contest, particularly when the administrator is also an officer of the sponsoring corporation or a closely related entity. Subsection (b)(1) requires that a trustee not deal with the assets of the plan "in his *own* interest." (Emphasis supplied.) *See Freund v. Marshall & Ilsley Bank*, 485 F. Supp. 629, 637 (W.D. Wis. 1979) (section 406(b) prohibits fiduciary from acting where personal interests may conflict with plan's interest). The question is how broadly "interest" should be read. While it would surely cover trustee interests of a financial nature, one commentator has argued that courts should not limit the section to financial interests:

> The absence of a direct financial interest in the transaction, however, should not preclude the application of this section to officer-trustees, as the prohibited transaction rules are designed to prevent the use of plan assets for any interest, financial or nonfinancial, other than an interest of the plan and its beneficiaries.

Note, *The Duties of Employee Benefit Plan Trustees Under ERISA in Hostile Tender Offers*, 82 COLUM. L. REV. 1692, 1703 n.51 (1982). In light of ERISA's broad language and protective provisions, we agree that we should read broadly the term "interest" in section 406(b)(1).[22] Thus, in a contest for corporate control, plan trustees who are also officers of either the "target" or the "raider" could be seen as having a significant "interest" of their own in the outcome of the contest. Officers of the "target" might well be immediately concerned about holding onto their jobs. Officers of the "raider" might find it in their interest, in terms of maintaining good relations with

[22] Where dealings between the fiduciary and the plan are necessary, the exemptions of 29 U.S.C. § 1108 will adequately protect the fiduciary.

their superiors, for example, to assist their corporation in its acquisition efforts.

C. *ERISA and the Reliable Trust Investments.* Under ERISA sections 404(a), 406(a)(1)(D) and 406(b)(1), where plaintiffs allege that fiduciaries have used plan assets for their own purposes in a corporate control contest, courts must examine closely the circumstances surrounding the alleged use of plan assets. In this case, several factors are relevant in deciding whether the plan administrators acted solely in the interests of the plan beneficiaries. First, the risk of conflicts between the interests of the fiduciaries and beneficiaries is the key warning signal for possible misuse of plan assets. Second, whether fiduciaries with divided loyalties make an intensive and scrupulous investigation of the plan's investment options may be highly probative of the fiduciaries' loyalties. Third, the consistent management of plan assets in congruence with the fiduciaries' personal interests over a substantial period of time in control contests may be probative of whether the fiduciaries have acted solely in the interests of the beneficiaries. This list is by no means exhaustive, but these are the factors applicable here.

On the record before us, we find that the district court clearly erred when it found that the Reliable Trust's investments in Berkeley, OSI and Hickory were made and held solely in the interests of the plan beneficiaries. We find that Dardick's and Zuckerman's investment of the trust's assets in Berkeley, OSI and Hickory violated ERISA's fiduciary requirements.

With regard to the Berkeley, OSI and Hickory investments, both Dardick and Zuckerman faced the clear risk of conflicting interests. As fiduciaries of the Reliable Trust, their duty was to promote the interests of the trust beneficiaries. Yet their ties to the Engle group and their involvement in the control contests gave them other interests which clearly could diverge from those of the beneficiaries. For example, as the Engle group began to expand its holdings, it benefited by keeping Berkeley,

OSI and Hickory stock prices as low as possible in the short run, thereby reducing the cost of its acquisition plans. The Engle group's success in the control contests depended upon the group's ability to control the largest possible block of shares.

The interests of Reliable Trust beneficiaries were markedly different. Their interests were best served by quickly rising stock prices, which often result from corporate control struggles. They certainly had no interest in preventing or delaying price rises. Further, the interests of the beneficiaries required disposing of the stock if it appeared that the investment had no further profit potential. Thus, if fully independent, the persons administering the trust might have wanted to sell the stock before the rest of the Engle group was in a position to cash in its own position. The beneficiaries were interested in the greatest possible return on their investment, regardless of whether their investments aided one side or another in a control contest. Further, independent trust administrators might have sold out earlier (or might never have bought in) if they believed that target management was acting contrary to the best interests of the stockholders.

Thus, as unpaid trust administrators, Dardick and Zuckerman faced responsibilities which could have conflicted sharply with the interests of the Engle group (upon which their income depended) in its control contests. Had a time come when a decision had to be made that would hurt the Reliable Trust and help Engle, or vice-versa, while Engle was effectively providing everyone's paycheck, we think it unrealistic to expect that the decision would not go in Engle's favor.[23] To the

[23] When the plaintiffs filed this action in September 1978, the potential conflicts may well have ripened into actual conflicts. The plaintiffs sought immediate distribution of their trust interests, and, as we discuss below in Part V, they may well have been entitled to immediate distribution. When the lawsuit

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extent the Reliable Trust and other entities in the Engle group were stockholders in the same target companies, they shared, of course, an interest in the ultimate maximization of the stock values. In that general sense, the interests were not in actual conflict. However, because the plaintiffs have shown that the trust administrators clearly faced potentially conflicting interests and continued to exercise control over the plan assets in ways that directly benefited the Engle group, grave doubts arise concerning the administrators' loyalty. Under these circumstances, it was virtually impossible for the plan fiduciaries to act with complete loyalty to the Reliable Trust beneficiaries and with an "eye single to the interests of the participants and beneficiaries." *Donovan v. Bierwirth*, *supra*, 680 F.2d at 271.[24]

Because of the other factors present in this case, we need not decide whether the potential conflicts alone amounted to ERISA violations. Where they faced these clearly conflicting loyalties, Dardick and Zuckerman un-

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[23] *continued*
was filed, the Reliable Trust still held its shares of OSI and Hickory, and the control contests for those companies were not over. Yet the trust administrators did not distribute most trust assets until after the control contests had ended. The district court found that the delays were reasonable, and we vacate that finding in Part V. On the record before us, we are reluctant to reverse the district court's finding and hold that the delayed distribution violated ERISA as a matter of law. We leave to the district court on remand the issues whether the fiduciaries' actions in delaying distribution violated the trust instruments or ERISA's standard of loyalty.

[24] The potential conflicts in the case before us seem, on the surface, at least, less severe than the one faced by the trust administrators in *Donovan v. Bierwirth*, where the administrators' positions in target management, and their presumed concern for their own jobs, might have been influences strongly adverse to the trust's interests as a stockholder. Nonetheless, the potential conflicts in this case were substantial enough to create the risk of misuse of plan assets.

dertook no genuinely independent investigation of the trust's investment options. At the very least they should have realized that their ties to the Engle group and their interests in the control contests cast serious doubt on their ability to act solely in the interests of the beneficiaries. Yet before the trust purchased the stocks and throughout the several control contests, Dardick and Zuckerman failed to seek independent advice which might have clarified where the interests of the beneficiaries lay.

Defendants contend that the trust's Berkeley purchases were prudent investments made upon the advice of the professional investment advisor, Charles Newbill. The reliance on Newbill's advice does not alter our conclusion that the investments were not made for the exclusive purpose of providing benefits to plan beneficiaries. On the contrary, in light of Newbill's ties to the entire Engle group, *see supra* Part I-A, his blessing of the trust's investments only adds support to the inference that the trust purchases were part of the Engle group's investment and acquisition program. First, at the time Newbill proposed the Berkeley investments to Dardick, Newbill's only paying client was Libco. The bill Newbill submitted to the Reliable Trust for the advice was prepared nine months after the purchases and three months after this lawsuit was filed. Newbill apparently made his recommendations in several conversations with Dardick during early 1978 and in several brief memoranda dated a few days before the trust made its purchases. *See* Defendants' Exhibits ZZ and AAA. Dardick and Zuckerman clearly knew of Newbill's involvement with Engle and Libco, and they were aware of Engle's and Libco's interest in the three companies. If Dardick and Zuckerman had been acting independently, we do not see how they could have failed to make their own investigation or to seek the advice of someone not involved in the Engle group's acquisition efforts.[25]

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[25] Defendants argue further that the Berkeley purchases, as well as those of OSI and Hickory, were prudent and made to di-

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Thus it is clear that the Reliable Trust investments in Berkeley, OSI and Hickory were made by administrators who faced conflicting loyalties and who made no effort to obtain independent advice regarding these investments and the interests of the trust beneficiaries. When we also examine the timing of the trust's investment decisions and their relationship to the actions of other members of the Engle group, it is clear that the trust's investments were not made with an "eye single" to the interests of the participants and beneficiaries. *Donovan v. Bierwirth*, *supra*, 680 F.2d at 271. Instead, the trust investments were made at least in part to enhance the Engle group's position in the several control contests.

The timing of the Reliable Trust purchases of Berkeley stock in relation to other actions of the Engle group shows that the trust assets were not used exclusively to further the interests of the trust beneficiaries. In late February 1978, Engle learned of the proposed deal between Berkeley management and the Cooper group trying to take over the company. At that time, Engle believed that the proposed deal would work to the disadvantage of minority

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[25] *continued*

versify the trust's assets. To support this claim, defendants point to the testimony of Lee Meyer, a Harris Bank officer, who testified that the Harris Bank had also purchased Berkeley shares in the Special Capital Fund it managed for many employee benefit plans. Defendants' Brief at 19, 38. However, Meyer also testified that the Special Capital Fund was "a highly speculative fund, high risk fund," and a "go-go fund." Transcript at 613, 620. He testified that the bank never put more than 5% of any single trust's assets in the Special Capital Fund because the investments were high risk. Transcript at 613. The narrow issue of prudence is not precisely before us on this appeal. However, the speculative nature of the Reliable Trust's investments and the fact that the investment in Berkeley apparently appreciated primarily through the use of litigation as an economic weapon indicate whether the plan administrators acted with unswerving loyalty to the trust beneficiaries.

shareholders such as himself and GSC. Although they faced the danger of being "locked-in" as minority shareholders under hostile management, Engle and GSC purchased an additional 11,200 shares between February 27th and March 10th, increasing the Engle group's Berkeley holdings from 3.5% to 4.0% by March 10th. Then, on March 22, 1978, letters were sent on GSC letterhead to the outside directors of Berkeley protesting the proposed Berkeley-Cooper deal. The letters were sent in Engle's name, but Dardick (who was, of course, at the same time the Reliable Trust administrator) prepared the letters and signed them for Engle. On April 7, 1978, Sierra, Engle and GSC filed suit against Berkeley and Cooper in the federal district court for the Northern District of Illinois. The complaint sought to enjoin the proposed deal, and Dardick prepared and signed the complaint. Thus, as attorney for Engle, Sierra and GSC, Dardick was arguing that Berkeley management was acting against the interests of minority shareholders, and he was suing management to stop the Berkeley-Cooper deal.

Meanwhile, between March 17th and March 31st, as administrators of the Reliable Trust, Dardick and Zuckerman were investing over $71,000 of the trust's assets in Berkeley stock. Under their direction, therefore, the Reliable Trust was becoming one of those minority shareholders against whose interests the Berkeley management was supposed to be acting. The Reliable Trust purchases of Berkeley stock increased the Engle group's block of Berkeley shares from 4.0% to 4.65% between March 17 and March 31, 1978. The suit by Engle, Sierra and GSC was settled in June 1978 by having Cooper Laboratories buy at a substantial premium the Berkeley shares owned by the Engle group. The Reliable Trust was not a party to the lawsuit, yet its Berkeley shares were also purchased as part of the settlement.[26]

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[26] Of course, Dardick could also have been criticized if the trust shares had *not* been included in the settlement, for then

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We believe that undisputed facts in the record show that the Reliable Trust investments in Berkeley were made at least in part for the benefit of other members of the Engle group in their effort to acquire a substantial block of Berkeley shares. Engle's response to the Berkeley-Cooper deal was to gain control of more Berkeley shares and to sue Berkeley management to force a favorable settlement. We can see no reason for including the Reliable Trust shares in the ultimate settlement unless the trust's shares were in fact subject to the Engle group's control in the contest for control of Berkeley. One reason for the trust purchases of Berkeley stock was to increase the Engle group's control of Berkeley and, from the perspective of the trust, to gamble on the outcome of the expected litigation and control contest. As we noted above in Part II, the fact that the gamble paid off for the trust as well as for the rest of the Engle group is no defense in this action for breach of fiduciary duties.

The Reliable Trust investments in OSI stock show a similar pattern. The trust made its investments in OSI very early in the struggle for control of OSI. Before Telco began purchasing OSI stock on April 17, 1978, GSC, Engle and the Reliable Trust owned a total of 24,100 shares, or 1.67% of OSI. The trust owned 12,500 of those shares. Beginning on April 17th Telco and later Telvest purchased OSI steadily, and the group's holdings grew to 6.2% by the end of May 1978, 9.7% by the end of July, 16% by the end of October, and 21.73% on May 4, 1979. Throughout the period of the Telco and Telvest purchases, the Engle group fought for control of OSI through litigation, two tender offers and a proxy fight. The Reliable Trust held its OSI shares during this time

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[26] *continued*

the trust would not have received the control premium offered by Cooper. The dilemma stems from the fact that Dardick owed a fiduciary's duty of loyalty both to the trust and to the other members of the Engle group whose interests potentially diverged from those of the trust.

and ultimately sold them for an enormous profit when the Brown Group tendered $15.00 per share as a "white knight" protecting OSI management.

Dardick acted as attorney for the Engle group in the proxy fight, the tender offers and the ancillary litigation. On behalf of the Engle group he was sharply critical of OSI management and the company's profitability. His efforts were aimed at forcing OSI management to yield control or to purchase the Engle group's shares at a premium. At the same time, Dardick directly controlled the Reliable Trust's investments in OSI, and he directed the Harris Bank to vote the trust's shares in the proxy fight in favor of the Engle group's candidates for the board of directors.

Like the Reliable Trust's Berkeley investments, the OSI investments were made, held and used while the Engle group was engaged in a struggle for corporate control against the incumbent management. The trust administrators and the Reliable Manufacturing board of directors were all deeply involved in those struggles. They had significant interests of their own at stake in the outcome of the struggle. Clearly there was no one who had discretionary authority over the trust investments and who was disinterested in the struggles for corporate control. And throughout the control struggle lasting over a year, the Reliable Trust held its OSI shares and used them in accord with the Engle group's best interests.

The Hickory investments display the same pattern, although Hickory management decided not to resist the Engle group's efforts to gain control of the company. Again, the administrators faced conflicting loyalties, at least until it became clear that the Engle group would be successful in its acquisition efforts. The Engle group wanted to keep the stock price down in the short run, while an independent trust would probably have been interested in quickly rising stock prices. Again, there was no effort to obtain independent advice on the soundness of the trust's purchase and retention of Hickory shares.

Throughout the long period during which the Engle group established its position in Hickory, the trust held its shares. Then, after it was clear that the Engle group would succeed, the trust sold its shares at a low point in the market for a net profit of 4%, including a loss on one-third of the shares it purchased. Under these circumstances, we conclude that the district court erred when it found that the defendants fulfilled their duties under ERISA.[27] Dardick and Zuckerman violated their duty of loyalty by investing the trust's assets in Hickory because they were not acting solely in the interests of the beneficiaries.[28]

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[27] The plaintiffs claim that defendants profited from their Hickory investments primarily through the use of "equity accounting," whereby as investors with "substantial influence" over Hickory, the defendants were able to include their share of Hickory's earnings in their own balance sheets. The district court found that the Reliable Trust's Hickory shares "played no part in the decision by, or ability of, Telco to use the equity method of accounting" with respect to its Hickory investments. Finding of Fact No. 15. That finding, which is not clearly erroneous, is relevant in determining whether and how the defendants profited from the trust's investments in Hickory. However, our conclusion that the investments violated ERISA's standard of loyalty does not depend upon the use of equity accounting or the extent of the profits made.

[28] Defendants point out that the trust made all of its Berkeley and OSI purchases, and most of its Hickory purchases, before Telco and Telvest made their larger purchases and before the contests for control began. They contend that these subsequent actions by other parties cannot transform the trust's earlier purchases into breaches of fiduciary duty. However, the argument misses the mark. First, before the trust made its purchases, other members of the Engle group had already begun to establish positions in the three companies, and Newbill was recommending the three companies to Engle and Libco as likely takeover candidates. Telco did not begin its larger purchases until April because it did not receive financing until shortly before the April 21st board meeting. Supplemental Ap-

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We conclude, therefore, that Dardick and Zuckerman violated their fiduciary duties under section 404(a), section 406(a)(1)(D) and section 406(b)(1) of ERISA by investing the Reliable Trust's assets in Berkeley, OSI and Hickory. We reach that conclusion because the fiduciaries had divided loyalties with clear potential for conflicts of interests, because the fiduciaries with divided loyalties failed even to seek independent, disinterested advice regarding these investments and their duties to the plan beneficiaries and because, throughout prolonged contests for corporate control, the fiduciaries' use of the trust assets dovetailed at all times with the interests of the Engle group.[29] Were we to reach another result in this case, we do not see how the interests of ERISA plan beneficiaries could be protected from those who would use trust property in contests for corporate control. The fiduciary's duty of loyalty is exacting, and the Reliable

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[28] *continued*

pendix at 425. Most importantly, though, a fiduciary's duty is not limited merely to purchases. During the control contests the administrators also faced the continual choice of holding or selling their shares in the contested companies. Where the administrators faced the conflicting loyalties present in this case, their actions in *holding* the shares had the effect of putting them in breach of their fiduciary obligations under ERISA. *See Donovan v. Bierwirth*, 680 F.2d at 272-74 (applying fiduciary standards to decisions to hold stock).

[29] We emphasize here that it is not *per se* impermissible for employee benefit plans to invest in companies involved in control contests or to ally themselves with one side or another in a control contest. The central issue is the *independence* of the plan fiduciaries who must always be able to act solely for the benefit of those whose funds are entrusted to them. In the case before us, where potential conflicts of interest are present, where the plan administrators are anything but independent and where these administrators fail to undertake any independent investigation of the investments, the long term congruence is additional evidence of the fiduciaries' breach of ERISA's duty of loyalty. The congruence alone would not demonstrate a breach of that duty of loyalty.

Trust administrators' use of the assets entrusted to them falls substantially short of that exacting standard.

Benefit plans subject to ERISA control an enormous pool of capital in today's economy. With their extensive investments in securities, they will frequently face difficult investment decisions in contests for corporate control. Therefore we emphasize that our finding of a breach of fiduciary duty in this case is predicated on the fiduciaries' intimate involvement with and interest in the other parties to the struggle for control. Where the plan fiduciary has interests outside the plan in a control struggle—interests which the benefit plan may be in a position to further or to impair—the risk is too great that the fiduciary will be unable to act as ERISA requires—solely in the interest of the plan beneficiaries.

As a practical matter, we view favorably the suggestion of the Secretary of Labor, as *amicus curiae*, that the preferred course of action for a fiduciary of a plan holding or acquiring stock of a target, who is also an officer, director or employee of a party-in-interest seeking to acquire or retain control, is to resign and clear the way for the appointment of a genuinely neutral trustee to manage the assets involved in the control contest.[30] Otherwise, the risk is too great that the trustee will come to a crossroads where the interests of the plan and the party-in-interest diverge. For example, while the party-in-interest may be seeking to accumulate as many shares as possible in order to maintain or acquire control, a plan's interest in maximizing its investment return may require it to tender its shares to a competing bidder for shares.[31]

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[30] It would not be necessary in all cases for the interested fiduciary to withdraw completely from plan management. The critical step is to have independent persons manage the assets involved in the control contest.

[31] Our holding in this case does not establish a *per se* rule based on potential conflicts of interest. We need not reach so far because here the fiduciaries with divided loyalties failed

(Footnote continued on following page)

The resignation of the interested fiduciary would also have the benefit of obviating in many cases the need for courts to sift through the complicated events surrounding a takeover in an attempt to gauge the prudence and motivations of trustees. Though neutral trustees will have the same fiduciary duties, we think it likely that the mantle of seeming objectivity worn by a neutral trustee will calm the fears of plan beneficiaries who might otherwise perceive the need to resort to the courts in order to ensure the safety of their entitlements.

IV.

We must also consider whether Clyde Engle and Libco are fiduciaries with respect to the Reliable Trust's investments and, if so, whether they breached their fiduciary duties. ERISA provides that:

> a person is a fiduciary with respect to a plan to the extent (i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets, (ii) he renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan. Such term includes any person designated under section 1105 (c)(1)(B) of this title.

29 U.S.C. § 1002(21)(A). The district court found that Engle did not have control or authority over the investment of plan assets except through his participation in the

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[31] *continued*

utterly to obtain independent advice from disinterested persons and because the trust's investment decisions were always congruent with the Engle group's interests. Nevertheless, we do not reject the *per se* standard here; should the proper case arise, we would need to decide the issue squarely.

appointment of the plan administrators. Finding of Fact No. 21. The court concluded that Engle and Libco were not fiduciaries with respect to the plan's administration and investment. Conclusion of Law No. 7.

Plaintiffs argue that Engle and Libco come within the scope of section 1002(21)(A)(iii), which makes one a fiduciary to the extent a person "has any discretionary authority or discretionary responsibility in the administration of [a] plan."[32] Plaintiffs contend that Engle and Libco had such discretionary authority over the plan by virtue of Engle's control of Libco and Libco's 100% ownership and control of Reliable Manufacturing: Libco had the power to appoint and remove the directors of Reliable (Engle, Zuckerman and Contarsy) who, in turn, had the power to appoint and remove the trust administrators (Dardick and Zuckerman). Therefore, plaintiffs argue, "By virtue of their ability to control appointments of Reliable Trust Administrators, Libco and Engle were fiduciaries." Brief of Appellants at 23.

It is clear that Engle and Libco are fiduciaries to the extent that they performed fiduciary functions in selecting and retaining plan administrators. ERISA recognizes that a person may be a fiduciary for some purposes and not others. The defendants contend that although Engle and Libco may be fiduciaries for the purpose of selecting and retaining plan administrators, that status does not make Engle and Libco fiduciaries with respect to the administrators' investment decisions.

Defendants' argument that ERISA ties fiduciary responsibilities to a person's actual authority is correct. The key language in the statutory definition is that a person is a fiduciary "to the extent" he or she exercises control or authority over the plan. The Secretary of Labor explained this language in a bulletin interpreting ERISA, which

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[32] Plaintiffs do not challenge on appeal the district court's conclusion that Telco and Telvest are not fiduciaries. *See* Brief for Appellants at 22-26.

was published in the Code of Federal Regulations. In this bulletin, the Secretary was asked the following question and gave the following response:

> D-4 Q: In the case of a plan established and maintained by an employer, are members of the board of directors of the employer fiduciaries with respect to the plan?
>
> A: Members of the board of directors of an employer which maintains an employee benefit plan will be fiduciaries only to the extent that they have responsibility for the functions described in section 3(21)(A) of the Act. For example, the board of directors may be responsible for the selection and retention of plan fiduciaries. In such a case, members of the board of directors exercise "discretionary authority or discretionary control respecting management of such plan" and are, therefore, fiduciaries with respect to the plan. *However, their responsibility, and consequently, their liability, is limited to the selection and retention of fiduciaries* (apart from co-fiduciary liability arising under circumstances described in section 405(a) of the Act). In addition, if the directors are made named fiduciaries of the plan, their liability may be limited pursuant to a procedure provided for in the plan instrument for the allocation of fiduciary responsibilities among named fiduciaries or for the designation of persons other than named fiduciaries to carry out fiduciary responsibilities, as provided in section 405(c)(2).
>
> The Internal Revenue Service notes that it would reach the same answer to this question under section 4975(e)(3) of the Internal Revenue Code of 1954.

ERISA Interpretative Bulletin 75-8, 29 C.F.R. § 2509.75-8 (1983) (emphasis supplied).

This court has adopted a similar approach to analyzing fiduciary responsibilities under ERISA. *Brandt v. Grounds*, 687 F.2d 895, 897 (7th Cir. 1982); *Chicago Bd. Options Exchange, Inc. v. Connecticut General Life Ins.*

Co., 713 F.2d 254, 259 (7th Cir. 1983). In *Brandt*, we affirmed the dismissal of an action against a bank that had allowed a plan trustee to withdraw $175,000 from the plan's accounts. The trustee had obtained the money by forging, or by obtaining under false pretenses, the signature of another trustee. In addition to alleging a breach of the bank's duties as a depository for accepting the forged instruments, plaintiffs alleged that the bank had breached its fiduciary duties under ERISA by acting imprudently in violation of the prudent man standard of 29 U.S.C. § 1104 (a)(1)(B). This court agreed that the bank may have been a fiduciary as a result of its providing investment advice for a fee, 29 U.S.C. § 1002(21)(A)(ii), but we held that "its fiduciary status existed only 'to the extent' that it provided that advice . . . . Thus, it appears that the personal liability of the Bank would be limited to its violations of 29 U.S.C. § 1104 in performing its investment advising functions." 687 F.2d at 897. The bank therefore was not a fiduciary with respect to its functions as a depository.

Similarly, in *Chicago Board*, we held that Connecticut General was a fiduciary because it had discretionary authority over management of plan assets by virtue of Connecticut General's power to amend its annuity contract with the Chicago Board Options Exchange. We noted, however, that Connecticut General's fiduciary status "only governs actions taken in regard to amending the contract and does not impose fiduciary obligations upon Connecticut General when taking other actions." 713 F.2d at 259.

Because Engle and Libco were fiduciaries with respect to the selection and retention of the plan administrators, the issue here is not whether they were fiduciaries but instead whether their fiduciary duties extended to the Reliable Trust investments in Berkeley, OSI and Hickory. The district court limited its analysis of this question to whether Engle and Libco directly exercised control over the Reliable Trust's investments. That analy-

sis was too limited in scope.[33] The fact that Engle and Libco had only limited fiduciary responsibilities does not

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[33] Under the district court's analysis, Engle and Libco were not fiduciaries with respect to the investments because plaintiffs did not show that Engle and Libco exercised direct control over the investments. On paper, it is true, Engle's authority over the Reliable Trust could be exercised only indirectly through his membership on the Reliable Manufacturing board which appointed the plan administrators. On paper, Libco could control the trust only through its power to appoint the Reliable Manufacturing board which in turn appointed the Reliable Trust administrators. However, we think ERISA directs courts to look beyond Engle and Libco's formal authority with respect to the plan, limited to selection and retention of administrators, and to consider what real authority they had over plan investments by virtue of their having appointed Dardick and Zuckerman to be administrators. *See Fulk v. Bagley*, 88 F.R.D. 153, 162 (M.D.N.C. 1980) ("in defining 'fiduciary' Congress was peculiarly concerned with realities, as distinguished from mere formalities."); *Eaves v. Penn*, 587 F.2d 453, 458 (10th Cir. 1978).

By selecting Dardick and Zuckerman to administer the plan, Engle and Libco presumably obtained substantial *de facto* control over plan investment decisions. Dardick was Engle's personal attorney and general counsel to the business enterprises controlled by Engle—Libco, Telco, Telvest, GSC, the Bank of Lincolnwood and Sierra. Most, if not all, of his income was under Engle's direct control. Further, while the Reliable Trust was investing in Berkeley, OSI and Hickory, Dardick was at the same time assisting Engle, Libco, Telco and Telvest in their acquisition programs and litigation against the same three companies. Dardick was thoroughly aware of how the Trust's investments would affect those acquisition programs. There would have been no need for Engle to instruct Dardick about how to use the trust assets. However, plaintiffs have not shown that the district court clearly erred in finding that Engle and Libco did not exercise authority over the trust's investments in Berkeley, OSI and Hickory. But the analysis here is more properly focused on whether Engle and Libco fulfilled the duties of surveillance and oversight which stemmed from their power to select and retain the plan administrators.

mean that they had no responsibilities whatever. As the fiduciaries responsible for selecting and retaining their close business associates as plan administrators, Engle and Libco had a duty to monitor appropriately the administrators' actions. 29 U.S.C. §§ 1104(a)(1), 1105(a) and 1105(c). *See* RESTATEMENT (SECOND) OF TRUSTS §§ 184, 224 (1959). Engle and Libco could not abdicate their duties under ERISA merely through the device of giving their lieutenants primary responsibility for the day to day management of the trust. Engle and Libco were obliged to act with an appropriate prudence and reasonableness in overseeing Dardick's and Zuckerman's management of the Reliable Trust. *Freund v. Marshall & Ilsley Bank*, 485 F. Supp. 629, 640 (W. D. Wis. 1979). *See also Shaw v. International Ass'n of Machinists and Aerospace Workers Pension Plan*, 563 F. Supp. 653, 657 (C.D. Cal. 1983).

The record shows that Engle was aware of the Reliable Trust's investments in Berkeley, OSI and Hickory, and that he also knew of Dardick's role and interest in the Engle group's acquisition efforts. He presumably should have been aware that Dardick—for whose appointment he was directly responsible—faced conflicting loyalties with respect to those investments. Engle also knew of Zuckerman's ties to the Engle group. Zuckerman was president of Reliable Manufacturing, a member of its board and administrator of the Reliable Trust, but he received no compensation for any of these positions. He was paid by Engle only as a consultant to Libco and as a member of the Libco board. Zuckerman thus had substantial interests of his own in the outcome of the Engle group's acquisition efforts, and Engle knew of those interests which created conflicting loyalties for Zuckerman as administrator of the Reliable Trust.

Libco was also aware of the Reliable Trust's investments and Dardick's and Zuckerman's conflicting interests. All three members of the Reliable Manufacturing board of directors—Engle, Zuckerman and George Contarsy—were also members of Libco's board of directors. Engle was chairman of the Libco board and

held a controlling interest in Libco. Libco, of course, controlled the Reliable Manufacturing board which appointed and oversaw the Reliable Trust administrators, who faced such markedly conflicting interests in managing the trust's investments. Documents filed by Libco with the Securities and Exchange Commission show that Libco knew of the Reliable Trust's investments in Berkeley, OSI and Hickory.[34]

The question thus becomes whether Engle and Libco fulfilled their duties under section 404 and section 405 in light of their knowledge that the Reliable Trust administrators who managed the trust assets faced conflicting loyalties with respect to those investments. Engle and Libco were not obliged to examine every action taken by Dardick and Zuckerman, but under these circumstances, we think that Engle and Libco were obliged to take prudent and reasonable action to determine whether the administrators were fulfilling their fiduciary obligations. Engle and Libco could not abdicate all of their responsibilities by appointing Dardick and Zuckerman, nor could they insulate themselves from all fiduciary liability by limiting their roles in the administration of the trust.

Nothing in the record now before us shows that Engle or Libco took steps either to insure that Dardick and Zuckerman were fulfilling their fiduciary obligations or to remedy any violations which might have already occurred. However, because the district court's analysis of this issue was so limited, the district court should consider this issue on remand so that the parties may address themselves directly to whether Engle and Libco acted reasonably and prudently in light of their knowledge of the administrators' conflicting interests and the trust's investments. Therefore, we vacate the district court's conclusion that Engle and Libco were not fiduciaries with respect to the trust's Berkeley, Hickory and OSI

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[34] *See supra* notes 11, 13 and 14.

investments, and we remand for further proceedings on the question of their liability as fiduciaries.

V.

Plaintiffs also allege that the Reliable Trust terminated as a matter of law, either wholly or partially, in March 1979 when Reliable Manufacturing discharged seventy-five of its eighty-one employees and went into involuntary and then voluntary bankruptcy proceedings. They claim that Dardick and Zuckerman as administrators and the National Boulevard Bank as trustee breached their fiduciary duties by delaying distribution of the trust after its legal termination.

The dispute over the termination of the plan and distribution of plan assets arose only after this litigation was initiated. On February 8, 1979, plaintiffs moved in the district court for appointment of a receiver to distribute vested funds in the Reliable Trust. In early March 1979, as noted, Reliable Manufacturing went into involuntary bankruptcy proceedings, and seventy-five of its eighty-one employees were laid off. Later in March, the bankruptcy proceedings were converted to voluntary proceedings under Chapter 11. Under applicable Internal Revenue Service regulations and the terms of the Reliable Trust instruments, the plan may have terminated when Reliable Manufacturing began to discharge its employees and went into bankruptcy, and the plan beneficiaries may have been entitled to an immediate distribution of their shares in the trust. *See* Plaintiffs' Exhibits 7 and 8; 26 C.F.R. § 1.401-6(1983). Beginning on March 1, 1979, attorneys for the Reliable Trust engaged in extended correspondence with the Internal Revenue Service seeking a determination of whether the trust had partially terminated. They described the lay-off of the seventy-five employees as "temporary" and "seasonal" in their letter to the IRS.

The district court denied the motion to appoint a receiver on May 30, 1979. Dardick and Zuckerman delayed distribution of the vested funds through the summer,

saying they were waiting for the IRS to advise them. Then, on September 14, 1979, Dardick and Zuckerman asked the district court to approve a notice to be sent to plaintiff beneficiaries. The proposed notice offered the plaintiffs the following choice. First, they could receive immediate payment of all vested funds, but only if they released the defendants from all liability, including liability in this case. Second, if they did *not* release the defendants from liability, the plaintiffs would receive their vested funds only over a ten-year period, subject to an unspecified reserve. The district court denied the defendants' request, and most trust funds were distributed in 1980 in return for releases not affecting rights in this case.

The district court found that the plan administrators acted reasonably in seeking the determination from the IRS and in setting aside a substantial reserve for attorney fees, accounting and other expenses. In its findings of fact and conclusions of law, the district court did not mention the attempt to make distribution of vested funds to plaintiffs contingent on a release from liability in this case. Nor did the district court address the proper application of the Reliable Trust instruments and the Internal Revenue Service regulations concerning termination of employee benefit plans. Further, the district court appears not to have considered the effect of the clear conflict of interests that crystallized when this litigation was filed. *See supra* note 23. Finally, the district court's findings of fact and conclusions of law are inconsistent in regard to the apparently important question whether the IRS determination was sought before or after the beginning of the bankruptcy proceedings.[35] Therefore, we

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[35] In its Finding of Fact No. 17, the district court said the defendants acted reasonably in seeking the IRS determination *before* bankruptcy proceedings began. In its Conclusion of Law No. 14, the court concluded that the defendants' decision to seek the IRS determination *subsequent* to the beginning of bankruptcy proceedings was not arbitrary or capricious. The precise timing of these events could be decisive in light of 26 C.F.R. § 1.401-6(b)(1)(1983) and § 9.1(b) of the agreement establishing the Reliable Trust.

vacate the district court's findings with respect to the delayed distribution of the Trust and damages which plaintiffs might have suffered from the delay. On remand the district court should consider when the Reliable Trust terminated and whether Dardick, Zuckerman and the National Boulevard Bank violated their fiduciary duties by delaying distribution of the Trust after bankruptcy proceedings had begun, by seeking an IRS determination regarding the termination of the plan, and by delaying distribution while seeking to make distribution contingent on releases from liability in this lawsuit. The court should also consider whether Engle and Libco fulfilled their fiduciary duties in overseeing the administrators' actions in delaying distribution. *See supra* Part IV. In addition, the court should also consider the extent, if any, to which plaintiffs may have been damaged by the delayed distribution of plan assets.

VI.

On remand the district court will face the formidable task of finding an appropriate measure of damages, if any, with regard to all defendants found to be liable as fiduciaries. Of course, the starting point for the inquiry is the language of 29 U.S.C. § 1109(a), which provides that:

> Any person who is a fiduciary with respect to a plan who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by this subchapter shall be personally liable . . . to restore to such plan any profits of such fiduciary which have been made through use of assets of the plan by the fiduciary. . . .

Plaintiffs contend that they are entitled to *all* profits made by Engle, Libco, Telco, Telvest, Dardick and Zuckerman in their own investments in Berkeley, OSI and Hickory. The plaintiffs' argument reaches too far, for it ignores the limiting words, "made through use of assets of the plan." 29 U.S.C. § 1109(a). We believe that this language of section 1109 permits recovery of a fiduciary's profits only where there is a causal connection between the use of the plan assets and the profits made by fiduciar-

ies on the investment of their own assets. *Cf. Brandt v. Grounds*, 687 F.2d 895, 898 (7th Cir. 1982) (plaintiffs must prove causal connection between plan losses and breaches of fiduciary duty). The Reliable Trust investments in Berkeley, OSI and Hickory were relatively small in proportion to the investments made by the whole Engle group.[36] If plaintiffs were to recover all profits made by all defendants in these transactions, the recovery could double or triple the size of the trust.

On remand the district court should determine whether the profits made by each defendant found to have breached his or its fiduciary duties are attributable, in whole or in part, to the Engle group's use of the trust and its assets. We recognize that in the context of a contest for corporate control, this inquiry into causation may be exceedingly difficult. Where, for example, the success and profitability of substantial minority investments depended upon the total amount of stock accumulated, it may be difficult to determine how much of the profit, if any, was attributable to the marginal increase in the group's block of shares contributed by the Reliable Trust. Also, the timing of the trust's investments may be relevant. Although the trust's investments in the three companies were small in

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[36] The table below shows the investments in Berkeley, OSI and Hickory by the Reliable Trust, investments by all members of the Engle group, including the trust, on April 16, 1978, before the Telco purchases, and the maximum holdings of the Engle group in each company. Percentages are percentages of each company's total outstanding shares.

	Berkeley	OSI	Hickory
Reliable Trust holdings	0.65%	0.87%	0.67%
Engle group holdings on April 16, 1978	4.64%	1.68%	4.88%
Maximum holdings of Engle group	10.70%	21.73%	52.80%

See Short Appendix at 29-33.

proportion to the Engle group's total investments in the companies, the trust investments were made very early in the control contests, when it may have been particularly valuable to acquire the first shares discreetly. We offer these observations, which are, of course, speculative, by way of suggestion to the district court in unravelling an extraordinarily difficult damages issue. There may well be other important considerations which the district court will discover when the parties present evidence which explores the issue of causation.

The problem of apportioning a wrongdoer's profits between those produced by his or her own legitimate efforts and those arguably resulting from his or her wrong is familiar to courts in other areas of the law. Where ERISA is silent as to how profits should be apportioned, we draw on those other areas of law for guidance. Perhaps the closest analogy is the apportionment of a copyright infringer's profits. The owner of a copyright may recover the infringer's profits, but only those attributable to the infringement and not to the infringer's own efforts and talents. *Sheldon v. Metro-Goldwyn Pictures Corp.*, 106 F.2d 45, 49 (2d Cir. 1939) (L. Hand, J.), *aff'd*, 309 U.S. 390 (1940). Where an infringer's profits are the product of both the infringer's own efforts and the infringement, a precise calculation is virtually impossible, yet justice requires that courts make estimates. In making an estimate, because the defendants are responsible for "mingling the plaintiffs' property with their own," doubts should be resolved against the defendants so that the amount awarded "will favor the plaintiffs in every reasonable chance of error." *Sheldon*, *supra*, 106 F.2d at 51.[37] Patent infringement de-

[37] When *Sheldon* was decided, the Copyright Act provided that the infringer would be liable for, among other things, "all the profits which the infringer shall have made from such infringement . . . ." 17 U.S.C. § 25(b) (1934). With respect to its causation element regarding profits, this provision is quite similar to the language of ERISA, 29 U.S.C. § 1109(a), which we apply here.

cisions under a prior statute with similar provisions requiring the disgorgement of profits took a similar approach to apportioning profits. *See Dowagiac Mfg. Co. v. Minnesota Moline Plow Co.*, 235 U.S. 641 (1915); *Westinghouse Elec. & Mfg. Co. v. Wagner Elec. & Mfg. Co.*, 225 U.S. 604 (1912).

This case is also similar to the common law problem in which a trustee commingles trust assets with his or her own so that it is difficult to discern which property and profits belong to whom. In a suit against the trustee, the trustee has the burden of showing which property and profits are his. The trustee is responsible both for the difficulty and for resolving it. *See* 5 A. SCOTT, THE LAW OF TRUSTS § 515 at 3612 (3d ed. 1967); 1 G. PALMER, THE LAW OF RESTITUTION § 2.13 (1978); *Grodsky v. Sipe*, 30 F. Supp. 656, 661 (E.D. Ill. 1940); *Winger v. Chicago City Bank & Trust Co.*, 394 Ill. 94, 111, 67 N.E.2d 265, 277 (1946).

Based on the treatment of these similar problems of apportionment, we believe that the burden is on the defendants who are found to have breached their fiduciary duties to show which profits are attributable to their own investments apart from their control of the Reliable Trust assets. It is conceivable that the defendants who have breached can show they received no benefit at all from use of the trust assets. In any event, while the district court may be able to make only a rough approximation, it should resolve doubts in favor of the plaintiffs. *Sheldon*, *supra*, 106 F.2d at 51.[38] This course should avoid the two unfair results of depriving defendants of the profits earned by their own efforts or depriving the plaintiffs of

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[38] The *Sheldon* rule was adopted in light of the common law of trusts. "[A]n infringer carries the burden of disentangling the contributions of the several factors which he has confused. The law requires him to resolve any doubts arising from his wrong; he is like any other constructive trustee." 106 F.2d at 48 (citing *Callaghan v. Myers*, 128 U.S. 617, 666 (1888)).

any recovery simply because the defendants have made it difficult to disentangle commingled profits.

We believe that this approach to the damages in this case is also in accord with the overall purpose of ERISA and the flexible remedial powers provided in 29 U.S.C. § 1109(a). The primary purpose of ERISA is to protect the interests of plan beneficiaries, and the disgorgement requirements of section 1109(a) are intended to promote their interests by removing the fiduciary's incentives to misuse trust assets. Yet that provision would be of little value if, in cases such as this, beneficiaries confronted an insurmountable obstacle in proving the extent of a fiduciary's profits. *See Brink v. DaLesio*, 667 F.2d 420, 426 (4th Cir. 1981) (burden of proof on trustee to show that prohibited transaction did not damage trust). We read section 1109(a), providing that the fiduciary "shall be subject to such other equitable or remedial relief as the court may deem appropriate," as authorizing us to cast the burden of proof on the defendants here to ensure that the disgorgement remedy is effective.

On remand, therefore, the district court should determine the extent of the defendants' profits, if any, made "through use" of the Reliable Trust assets. In doing so it must remember that the need for apportionment arose on account of defendants' breaches of their fiduciary duties. Plaintiffs must be denied a windfall but must receive the benefit of such reasonable doubts as appear.

In addition, some defendants may be liable as fiduciaries for damages resulting from delays in distribution. *See supra* Part V.

VII.

The district court also awarded costs and fees to all defendants, and it found that Dardick, Zuckerman and the National Boulevard Bank were entitled as fiduciaries to reimbursement for costs and attorneys' fees from the assets of the Reliable Trust. One law firm has represented all defendants in this case. The awards of costs and attorneys' fees to all defendants cannot stand.

ERISA provides that the district court in its discretion may award attorneys' fees to any party, 29 U.S.C. § 1132(g)(1), but the court's discretion is not unbounded. The courts have developed standards for the exercise of their discretion in awarding attorneys' fees under ERISA.[39] The district court made no findings and apparently undertook no analysis that would justify an award of fees to any defendants. From the record we can discern no grounds for the district court's fee award, and therefore we would have to vacate the award to all defendants even if we were to affirm the district court's judgment on the merits. *Cf. Janowski v. International Brotherhood of Teamsters Local No. 710 Pension Fund*, 673 F.2d 931, 941 (7th Cir. 1982) (upholding fee award where basis for award could be discerned from record), *vacated on other grounds*, 103 S. Ct. 3565 (1983).

In any event, because we hold that Dardick and Zuckerman violated their duties to administer the Reliable Trust solely in the interest of the beneficiaries, we reverse the award of fees and costs for those defendants. Where an ERISA beneficiary substantially prevails on the merits of

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[39] In deciding whether to award fees, the court should consider several factors, including:

> (1) The degree of the opposing parties' culpability or bad faith; (2) the ability of the opposing parties to satisfy an award of fees; (3) whether an award of fees against the opposing parties would deter others from acting under similar circumstances; (4) whether the parties requesting fees sought to benefit all participants and beneficiaries of an ERISA plan or to resolve a significant legal question regarding ERISA; and (5) the relative merits of the parties' positions.

Marquardt v. North American Car Corp., 652 F.2d 715, 717 (7th Cir. 1981) (quoting *Hummell v. S. E. Rykoff & Co.*, 634 F.2d 446, 452 (9th Cir. 1980)). Even where the plaintiff does not prevail on his or her claim, an award of attorneys' fees against an ERISA plaintiff will rarely be justified. *See Marquardt, supra*, 652 F.2d at 719-20.

his or her claim, an award of fees with respect to such a claim against the party in question would almost always be an abuse of discretion. *See Miles v. New York State Teamsters Conference*, 698 F.2d 593, 602 (2d Cir.) (vacating award of fees to plaintiffs where judgment for plaintiffs was reversed on appeal), *cert. denied*, 104 S. Ct. 105 (1983); *Kemmis v. McGoldrick*, 706 F.2d 993, 997-98 (9th Cir. 1983) (vacating fee award to employer where judgment for employer was reversed on appeal).

Because we vacate the district court's conclusions that Engle, Libco and the National Boulevard Bank are not liable as fiduciaries, we also reverse the award of fees and costs to them. Plaintiffs may still show that these defendants breached their duties to the trust and its beneficiaries, so any award of fees is premature. Also, even if Engle, Libco and the bank had prevailed on the merits, the district court's failure to establish a basis for the fee award and the problems of apportionment where one firm of attorneys represents all defendants would require us to vacate the fee award to these defendants.

Plaintiffs have not prevailed on the merits against Telco and Telvest, but we must vacate the award of attorneys' fees to Telco and Telvest. As we noted above, because the district court failed to analyze the factors relevant for awarding fees under ERISA, there is no basis in the record for the award of fees to Telco and Telvest. Further, because all defendants in this case were represented by one law firm, and because we reverse the award of fees to Dardick, Zuckerman, Libco, the bank and Engle, it is now impossible to determine Telco's and Telvest's shares of the total defense costs. In any event, we question whether the factors relevant to ERISA fee awards would justify a fee award for Telco and Telvest. Therefore, we vacate this award and leave all other matters involving fee determinations—whether in favor of defendants or in favor of plaintiffs—for the district court on remand.

SUMMARY

Our treatment of the district court's findings may be summarized as follows. First, we reject the conclusion that Dardick and Zuckerman did not violate their fiduciary duty to act solely in the interests of plan beneficiaries and find to the contrary. We hold that as a matter of law, the investments in OSI, Berkeley and Hickory were not made for the exclusive benefit of the plan beneficiaries. We also vacate the district court's conclusion that Engle and Libco were not liable as fiduciaries with respect to the investments and leave further fact-finding in this respect to the district court.

With regard to the delayed distribution of remaining plan assets, we vacate the district court's findings that the delays were reasonable and did not injure the plaintiffs. On remand the district court should consider whether the delays were proper and whether plaintiffs were damaged in any way by the delayed distribution of their vested funds in the trust. The court should also consider whether Engle and Libco fulfilled their duties with regard to the delayed distribution. In addition, the district court should consider at the first opportunity the desirability of an immediate distribution of all remaining assets in the Reliable Trust.

We reverse the district court's award of attorneys' fees and costs to Dardick, Zuckerman, Engle, Libco and the National Boulevard Bank. We vacate the fee awards to Telco and Telvest. Finally, the district court on remand will need to consider the question of damages with respect to each defendant found to have violated the fiduciary duties imposed by ERISA.

VACATED AND REMANDED.

A true Copy:

Teste:

Clerk of the United States Court of Appeals for the Seventh Circuit

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United States Court of Appeals

For the Seventh Circuit
Chicago, Illinois 60604

March 20, 1984.

Before

Hon. HARLINGTON WOOD, JR., Circuit Judge
Hon. RICHARD D. CUDAHY, Circuit Judge
Hon. ROBERT A. GRANT, Senior District Judge*

CHARLES W. LEIGH
and ERVIN F. DUSEK, etc.
Plaintiffs-Appellants,
and
GEORGE JOHNSON, et al.,
Intervening Plaintiffs-Appellants,
vs.
Nos. 82-2943
and
82-3040
CLYDE WILLIAM ENGLE, et al.,
Defendants-Appellees.

Appeals from the United States District Court for the Northern District of Illinois, Eastern Division.

No. 78 C 3799

George N. Leighton, Judge.

ORDER

The opinion in the above-entitled case, issued January 27, 1984, is modified by adding the following as a new paragraph at the end of footnote 25 on page 31 thereof.

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*Honorable Robert A. Grant, Senior District Judge for the Northern District of Indiana, is sitting by designation.

> Additionally, defendants point out that the Reliable Trust's investments had all been held in the form of fixed income securities until March 1978, and that they were required to diversify these holdings. *See* 29 U.S.C. §1104(a)(1)(C). We do not question the need for diversification; in the abstract, it was entirely proper for the trust to purchase common stocks. However, the problem in this case is the particular choice of stocks in light of the other defendants' holdings in Berkeley, OSI and Hickory, and in light of the administrators' own interests, previously discussed, in these companies. A general need or desire for diversification cannot serve to justify the choice of the stocks purchased in this case.

On consideration of the petition for rehearing and suggestion for rehearing *in banc* filed in the above-entitled case, no judge in active service has requested a vote thereon, and all of the judges on the original panel have voted to deny the rehearing. Accordingly,

IT IS ORDERED that the aforesaid petition for rehearing be, and the same is hereby, DENIED.

IN THE UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

CHARLES W. LEIGH and
ERVIN F. DUSEK,
Plaintiffs,

GEORGE W. JOHNSON,
ELEANOR MADSEN, et al.,
Intervening Plaintiffs,
vs.
CLYDE WILLIAM ENGLE,
NATHAN DARDICK, RONALD
ZUCKERMAN, LIBCO CORPORATION, TELCO MARKETING
SERVICES, INC., TELVEST, INC.,
NATIONAL BOULEVARD BANK
OF CHICAGO, and THE RELIABLE
EMPLOYEES' PROFIT SHARING
PLAN TRUST,
Defendants.

No. 78 C 3799

Before the Honorable
George N. Leighton
United States
District Judge

Memorandum

This civil action, brought under the provisions of the Employee Retirement Income Security Act of 1974, commonly known by the acronym ERISA, 29 U.S.C. §§1001, *et. seq.*, has been tried to the court. In pretrial proceedings, intervening plaintiffs have entered the suit and filed a pleading; a class has been certified. Over a span of eight and one-half days, evidence of events which occurred almost 14 years ago has been heard, volumes of exhibits have been received, counsel for the parties have presented oral arguments, written post-trial submissions have been made; and the court, pursuant to Rule 52(a), Fed. R. Civ. P., files this memorandum of its findings and conclusions.

I. Findings of Fact

(1) Reliable Manufacturing Corporation's Employees' Profit-Sharing Plan was created on December 23, 1968. Plaintiffs Charles W. Leigh and Ervin F. Dusek formerly owned 100% of the shares in, and were officers and directors of Reliable Manufacturing Corporation; from inception of the plan until September 15, 1977, they were its administrators. The remaining plaintiffs, all intervenors in this suit, constitute a class of former employees of Reliable Manufacturing Corporation who have funds in the plan.

(2) Defendant Libco Corporation purchased Leigh and Dusek's 100% interest in. Reliable on April 5, 1977; and later that same year, Libco filed a suit in this court, docketed as 77 C 4386, seeking damages in excess of $2,000,000 and rescission of the purchase contract on alleged grounds of common law fraud and violations of Section 10(b) of the Securities Exchange Act of 1934, Rule 10(b) promulgated thereunder, as well as Section 17 of the Securities Act of 1933. On September 15, 1977, defendants Nathan H. Dardick and Ronald Zuckerman were appointed by the board of directors of Reliable to replace Leigh and Dusek as the committee to administer the plan; they have served continuously to the present, and as had Leigh and Dusek, without compensation or reimbursement. Defendant Clyde W. Engle has been and is an officer and director of defendants Libco Corporation, Technical Equipment Leasing Corporation, formerly known as Telco Marketing Services, Inc. After Libco purchased Reliable Manufacturing Corporation, he became a director of Reliable. Defendants Telco and Telvest are subsidiaries of the defendant Libco. Defendant National Boulevard Bank has been trustee of the plan since February 5, 1979.

(3) From 1968 to approximately mid-1975, Harris Bank in Chicago invested the plan's assets Harris considered a prudent diversification of assets to be approximately 55% common stock and 45% fixed income securities.

(4) Following a period in 1974 when, through investments by Harris, the plan lost approximately 18% in the market value of its assets, plaintiff Charles W. Leigh, the responsible plan administrator, directed Harris to no longer invest any new assets of the plan in common stocks. In February 1976, Leigh directed all of the plan's assets to be transferred to the bank's Investment Reserve Fund, where they remained until early 1978. Leigh had no investment experience and his decision to invest all of the plan's assets in the Investment Reserve Fund was contrary to the investment advice of Harris which continued to recommend that approximately 55% of the plan's assets remain invested in common stocks.

(5) Following their appointment as the plan's committee on September 15, 1977, defendants Dardick and Zuckerman retained the law firm of Sachnoff, Schrager, Jones, Weaver & Rubenstein to revise the plan in order to bring it into conformity with ERISA. The plan was revised and submitted to the IRS in late December 1977; and, with minor modifications, it was approved by the IRS on July 24, 1978.

(6) Section 1.3 of the plan, entitled "Power to Direct Investments" provides as follows:

> The Committee shall have the power to direct the Trustee with respect to all investments of the principal and income of the Trust Fund. In connection with such power, the Committee may employ investment counsel.

Accordingly, the Committee directed Harris Bank to invest approximately 60% of the plan's assets in short term fixed-income securities, and Charles Newbill was retained as an investment advisor to recommend common stock investments for the remainder of the plan's portfolio. Mr. Newbill is an experienced financial analyst. After making a detailed analysis of possible and prudent investments, Mr. Newbil, early in 1978, reported to the plan administrators that certain common stocks were undervalued in

the marketplace with little downside risk and a strong likelihood of upside potential. He recommended that the plan invest in the common stock of: (1) Outdoor Sports Industries, Inc., (2) Berkeley Bio-Medical Incorporated; (3) Hickory Furniture Company; and (4) Dixon Joseph Crucible Company.

(7) Acting on this advice, the plan purchased and sold common stock in the following corporations:

	Date of Purchase	Date of Sale	No. of Shares	Total Cost/ Sale Price	Total Profit To Plan	Return on Investment
Outdoor	3/22/78		1,400			
	3/23/78		2,500			
	3/29/78		2,100			
	3/30/78		1,500			
	3/31/78		4,900			
	4/14/78		100			
			12,500	$77,736.83		
		6/26/79	12,500	187,500.00	$109,763.17	141%*
Berkeley	3/17/78		10,000			
	3/21/78		1,500			
	3/23/78		1,500			
	3/27/78		1,000			
	3/31/78		1,800			
			15,800	$71,580.53		
		8/18/78	15,800	118,500.00	$ 46,919.47	66%
Hickory	3/22/78		8,000			
	6/9/78		4,000			
			12,000	$72,433.21		
		3/19/79	12,000	75,000.00	$ 2,566.79	4%*
Dixon	9/14/78		1,000			
	9/15/78		1,000			
			2,000	$72,453.21		
		3/19/79	2,000	75,000.00	$ 2,546.79	4%*

* Exclusive of dividends received

(8) The plan also purchased and sold $50,000 in face amount Bank of Lincolnwood Capital Notes as follows:

Summary of Reliable Profit Sharing Plan's
Investment in Bank of Lincolnwood Capital Notes

Disbursements from plan for capital notes

$20,000 Capital Note purchased 7/12/78

Gross Amount	$16,600.00
Accrued Interest	505.28
Tax	.95
Total disbursed from plan-7/26/78	$17,106.23

$30,000 Capital Note purchased 9/22/78

Gross Amount	$25,500.00
Accrued Interest	1,260.83
Total disbursed from plan-1/11/79	$26,760.83

Total disbursements from plan for notes	$43,867.07

Receipts by plan from capital notes

Interest on notes received by plan:

1/16/79 ($20,000 note)	$ 850.00
4/24/79 ($30,000 note)	1,275.00
Interest received on notes	$ 2,125.00

$50,000 in capital notes sold 7/31/79

Principal	$42,125.00
Accrued Interest	1,475.70
Total Proceeds of Sale	$43,600.60

Total receipts by plan for notes	45,725.70
Excess of receipts over disbursements	$ 1,858.64

(9) The performance of the plan's challenged investments in the common stock of Outdoor Sports Industries, Inc., Berkeley Bio-Medical Incorporated and Hickory Furniture Company can be summarized as follows:

Summary of Reliable Profit Sharing Plan's Challenged Investments

	Amount Invested	Selling Price
Berkeley Bio-Medical, Inc.	$ 71,580.53	$118,500.00
Hickory Furniture Company	72,433.21	75,000.00
Outdoor Sports Ind., Inc.	77,736.83	187,500.00
	$221,750.57	$381,000.00
Profit to plan		$159,249.43
Return on investment (exclusive of dividends received)		72%

These investments were made with plan assets and all profits were received by the plan.

(10) Purchases of all of these securities were made through stock brokers in the open market, and all of the securities were kept in the possession of the plan trustees. No plan moneys were ever disbursed for these securities until the stock certificates or capital notes were received. The plan's Hickory Furniture Company and Joseph Dixon Crucible common stock, and its Bank of Lincolnwood capital notes, were sold through stock brokers in the open market.

(11) The plan's Berkeley Bio-Medical common stock was sold at $7.50 per share at a time when the market price of the stock was between $5 and $6 per share. This advantageous sale by the trust was made possible by Mr. Dardick's insistence that the plan's stock be included in the sale pursuant to a settlement agreement of certain litigation involving Berkeley Bio-Medical, Telco and Mr. Engle. The plan was permitted to sell its stock at $7.50

per share even though it was not a party to the litigation and none of its assets were used to pay any part of that litigation. The plan's Outdoor Sports Industries, Inc. common stock was sold at $15 per share pursuant to a tender offer by the Brown Group, Inc. All of these investments were made with plan assets, and all profits were received by the plan. Assets of the plan were used for the exclusive benefit of the plan; beneficiaries of the plan were benefitted by these investments.

(12) Investments by the plan in the common stock of Hickory, Berkeley and OSI were to diversify the plan's investment portfolio. Dardick's reliance on Charles Newbill's investment advice was reasonable; there was no impropriety in the plan retaining its investments in Berkeley, Hickory and OSI after Telco also made major purchases in the stock of these companies. the purchases by Telco of common stock in these companies at prices greater than the plan had paid for its shares and after the plan's purchases, operated to benefit the plan. The plan's investment decisions in the foregoing stocks were made by Nathan H. Dardick following consultation with and recommendations by Charles Newbill.

(13) The plan's investments in the foregoing stocks were prudent. Dardick, as the responsible plan administrator, gave appropriate consideration to:

A. composition of the plan's assets with regard to diversification;

B. liquidity and current return on the plan's assets relative to the anticipated cash flow requirements of the plan;

C. projected return on the plan's assets in light of the funding objectives of the plan; and

D. particular investments in light of the purposes of the plan, taking into consideration the risk of loss and opportunity for gain associated with the investments.

No loss or damage was sustained by the plan, or by any of the plaintiffs, as a result of the plan's investments in Berkeley, Hickory and OSI. In fact, the plan and its participants benefitted from these investments. At no time did defendants Engle, Libco, Telco or Telvest use the assets of the plan for accounting or other purpose. At no time have any assets of the plan, including its purchases of Hickory Furniture Company, Outdoor Sports Industries, Inc. or Berkeley BioMedical, Inc. common stock, been reflected in the accounting records of Libco Corporation, Telco, or their subsidiaries (including Telvest, Inc.) for any purpose.

(14) The equity method of accounting was never applied by Libco Corporation, Telco or their subsidiaries (including Telvest, Inc.) to their purchases of stock in Outdoor Sports Industries, Inc. and Berkeley Bio-Medical, Inc.

(15) Telco did treat its ownership of Hickory Furniture Company stock on the equity method of accounting commencing August 1, 1978, based upon its own direct ownership of common stock of Hickory Furniture Company and its representation on the board of Hickory Furniture Company at that time. The decision by Telco to apply the equity method of accounting to its ownership of Hickory Furniture Company common stock is consistent with Accounting Principles Board Opinion No. 18. Ownership of Hickory Furniture Company common stock by the Reliable Profit Sharing Plan Trust played no part in the decision by, or ability of, Telco to use the equity method of accounting. The accounting records of the plan were separately maintained by the accounting firm of Berman & Berman.

(16) As of December 30, 1977, the plan's assets totaled $729,526.32. Plaintiffs have been paid $991,478.89 by the plan in distributions after the time defendants Dardick and Zuckerman became plan administrators.

(17) The plan trustee, and the plan administrators, acted reasonably in seeking a determination from the Internal Revenue Service beginning March 1, 1979 as to whether a partial termination of the plan had occurred by reason of the substantial layoff of Reliable Employees. An involuntary bankruptcy petition was filed against Reliable Manufacturing Corporation in early March 1979 and was converted to a Chapter 11 reorganization in mid-March 1979. Reliable Manufacturing Corporation was adjudicated as bankrupt on December 6, 1979. Plan administrators acted properly in setting aside a reserve of approximately $100,000 for use as attorney's fees, accounting and other administrative expenses pending the final outcome of this litigation.

(18) Plan assets have been used exclusively in the interest of its beneficiaries. Plan administrators, and the plan trustee, have not, in any way, acted arbitrarily or capriciously in distributing assets of the plan to the plaintiffs. Plaintiffs have not proved any damage sustained by any of them as a result of any claimed delay in the payment to any of them of their individual share in the plan.

(19) The delay in the payment to plaintiffs of their share in the plan has been caused by the following factors or events:

A. The economic condition of Reliable Manufacturing Corporation during the period ending on or about March 1, 1979 with the lay-off or discharge of 75 out of 81 of the Intervenors and class members, and the filing by Reliable's creditors of an involuntary petition in bankruptcy against the company;

B. The posture of litigiousness that existed between Leigh and Dusek and the Libco Corporation as a result of the suit in 77

C 4386 which accused Leigh and Dusek of fraud in their sale of Reliable to Libco;

C. The filing of the suit in this case by Leigh and Dusek, represented by a lawyer who apparently developed an emotional involvement in the dispute between the parties, and who furnished the legal and factual theory for this litigation.

Such delay as has occurred in the payment to the plaintiffs of their share in the plan can be reasonably traced to the factors or events described. Dardick and Zuckerman, in the discharge of their fiduciary duties as plan administrators, have acted in accordance with the terms of the plan, and within the discretion vested in them as the plan's administrators.

(21) Clyde Engle did not, at any time, exercise any control respecting management or disposition of plan assets; nor did he have any authority or responsibility to do so, other than as one of three members of the Reliable Manufacturing Board of Directors, participated in appointing the plan's administrators. After having participated in this appointment, Engle did not, at any time or in any way, have any part in the administration of the plan or in decisions concerning investment of plan assets.

(22) The profits made by Libco, Telco and Telvest in Outdoor sports, Berkeley Bio-Medical and Hickory Furniture were made through the use of their own assets; no basis in the evidence exists to deprive these publicly held companies or their shareholders of their profits.

(23) Clyde W. Engle, Ronald Zuckerman and Nathan H. Dardick, from their demeanor on the stand, their manner of testifying, the facts and circumstances which have come to this court's attention in the course of this litigation, and from other evidence in the record, were highly credible witnesses. They gave this court the sense impression that

they are conscientious and knowledgeable individuals. In particular, Dardick's decisions with respect to the investments were motivated by a sincere desire to seek prudent investments for the exclusive benefit of the plan beneficiaries. The statements by Lee Meyer, Glenn Torgerson and Albert Weiss to the effect that at no time were any of the plan's assets used or attempted to be used for any improper purpose were highly probative of the good faith of the plan's administrators. Moreover, it is of evidentiary significance that no plaintiff has come forward to testify in support of any allegation contained in the complaint filed by the lead plaintiffs Leigh and Dusek, or those contained in the complaint of the intervenors. The only apparent theory of evidentiary support for the allegations of ERISA violations was the reading of volumes of documents by the lawyer for Leigh and Dusek, documents consisting mainly of 13D's filed by defendants, or some of them, with the Securities and Exchange Commission in accordance with law.

(24) Nathan H. Dardick and Ronald Zuckerman, as the plan's administrators, have used plan assets to pay for the legal defense of this action, including payment of attorney fees. Disbursements by defendants of plan assets in this manner have been made necessary by the needs of this lawsuit, instituted as it has been, by Leigh and Dusek, and joined in by the intervenors.

II. Conclusions of Law

From these facts, the court reaches the following conclusions of law.

(1) Under the provisions of 29 U.S.C. §1132(c), it has jurisdiction over the parties and the subject matter of this litigation.

(2) Defendants Zuckerman, Dardick and National Boulevard Bank are fiduciaries as defined in 29 U.S.C. §1002(21) (A).

(3) Defendants Clyde William Engle, Libco, Telco and Telvest are "parties in interest" as defined in 29 U.S.C. §1002(14).

(4) Application of 29 U.S.C. §1104 to §1106, shows that defendants Dardick, Zuckerman, and National Boulevard Bank have not breached their fiduciary duties to the plan by reason of the investments in question.

(5) Application of 29 U.S.C. §1104 and 29 C.F.R. §2250.404a-l show that all of the investments by the plan administrators were prudent.

(6) The investments by the plan administrators did not constitute prohibited transactions as defined in 29 U.S.C. §1106.

(7) Defendants Engle, Libco, Telco, and Telvest are not fiduciaries of the plan with respect to its investments or its administration, as that term is defined in 29 U.S.C. §1002(21) (A). This statute provides that a person is a fiduciary with respect to a plan "to the extent (i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets, (ii) he renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan." Neither Engle, Libco, Telco, or Telvest falls within the plain and easily understood language of (i), (ii), or (iii) of 29 U.S.C. §1002(21) (A).

(8) No provision of ERISA prohibits a person from being a fiduciary when he or she is also an officer, employee, agent, or other representative of a party in interest. In fact, 29 U.S.C. §1108(c) (3) expressly provides that "[n]othing in section 1106 of this title shall be construed to prohibit any fiduciary from-serving as a fiduciary in addition to

being an officer, employee, agent, or other representative of a party in interest."

(9) The purchase of the Bank of Lincolnwood capital notes did not constitute a prohibited transaction either under 29 U.S.C. §1106(a)(1) (E), 29 U.S.C. §1107, or any other provision of ERISA.

(10) ERISA creates no cause of action where the plan has not been damaged. *Alton Memorial Hospital v. Metropolitan Life Insurance Company*, 656 F.2d 245, 249 (7th Cir. 1981). Neither the named plaintiffs nor the intervenor plaintiffs have produced any evidence that the plan has been damaged by any act of commission or of omission by any defendant in this suit.

(11) Under 29 U.S.C. §1104(a) (1) (A) which provides that "a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and – for the exclusive purpose of defraying reasonable expense of administrating the plan;. . ." and 29 U.S.C. §1108(c) (2) which in pertinent part provides that "[n]othing in section 1106 of this title shall be construed to prohibit any fiduciary from --receiving . . . reimbursement of expenses properly and actually incurred, in the performance of his duties with the plan. . .", use of plan assets by defendants Dardick and Zuckerman as plan administrators to pay for the expenses which they have incurred in the defense of this action was proper and consistent with the letter and spirit of applicable sections of ERISA. Accordingly, from the funds in their possession, they have the right to pay for all such expenses, including attorney's fees reasonably incurred by them in the defense of this action brought by the named plaintiffs, and joined in by the intervenor plaintiffs.

(12) Defendants Dardick, Zuckerman and National Boulevard Bank did not breach any of their co-fiduciary obligations under 29 U.S.C. §1105(a) (1)-(3).

(13) The purchase and sale of Bank of Lincolnwood capital notes did not involve the purchase or sale of an employer security as defined by either 29 U.S.C. §1106(a)(1)(E) or 29 U.S.C. §1107(d)(7).

(14) The decisions of the plan trustee and administrators to seek a determination from the IRS subsequent to the institution of a Chapter 11 proceeding by Reliable Manufacturing Corporation was not arbitrary or capricious conduct as plan fiduciaries.

(15) It is clear to this court that plaintiffs have not met the burden which was theirs to prove that the actions of the plan administrators were arbitrary and capricious. Even if the plan administrators had the burden of justifying their actions, they and the trustee have met their burden of demonstrating that all of their actions were prudent and were done for the exclusive benefit of the plan and its beneficiaries.

(16) Therefore, defendants Clyde William Engle, Nathan Dardick, Ronald Zuckerman, Libco Corporation, Telco Marketing Services, Inc., Telvest, Inc., and National Boulevard Bank of Chicago, are entitled to judgment in their favor and against the named plaintiffs Charles W. Leigh, Ervin F. Dusek, and the intervenor plaintiffs, George W. Johnson and Eleanor Madsen, et al. Costs, expenses, and fees are to follow the judgment as provided by law as to each defendant. Defendants Dardick, Zuckerman, and National Boulevard Bank, plan administrators and trustee, respectively, are entitled to be reimbursed from or pay out of plan assets, their reasonable costs, expenses and fees, including those they have paid or are obliged to pay for attorney's fees in defending this legal action. A judgment order in conformance with Rule 58, Fed. R. Civ. P., will be entered; execution to follow.

So ordered,
/s/ GEORGE N. LEIGHTON
George N. Leighton
United States District Judge

Dated: NOV 18 1982

IN THE UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

CHARLES W. LEIGH and
ERVIN F. DUSEK,
Plaintiffs,

GEORGE W. JOHNSON,
ELEANOR MADSEN, et al.,
Intervening Plaintiffs,
vs.

CLYDE WILLIAM ENGLE,
NATHAN DARDICK, RONALD
ZUCKERMAN, LIBCO CORPORATION, TELCO MARKETING
SERVICES, INC., TELVEST, INC.,
NATIONAL BOULEVARD BANK
OF CHICAGO, and THE RELIABLE
EMPLOYEES' PROFIT SHARING
PLAN TRUST,
Defendants.

No. 78 C 3799

Before the Honorable
George N. Leighton
United States
District Judge

Judgment

This cause having been heard to the court, evidence consisting of testimony and documents having been admitted, post-trial oral and written submissions made; and the court having made its findings of fact and reached its conclusions of law, it is adjudged that judgment be and the same is entered in favor of defendants Clyde William Engle, Nathan Dardick, Ronald Zuckerman, Libco Corporation, Telco Marketing Services, Inc., Telvest, Inc., and National Boulevard Bank of Chicago, and against the named plaintiffs, Charles W. Johnson and Eleanor Madsen, et al., said plaintiffs and intervenors to take nothing by their complaints. Costs, expenses, and fees are to follow the judgment of each defendant, as provided by law as to each of them.

Defendants Dardick, Zuckerman, and National Boulevard Bank of Chicago, plan administrators and trustee, respectively, may recover from plan assets in their possession their reasonable costs, expenses, and fees, including those they have paid or are obliged to pay in defending this legal action. Defendants, each of them, as provided by law, to have execution for such costs, expenses, and fees, as by law determined.

So ordered,

/s/ GEORGE N. LEIGHTON
George N. Leighton
United States District Judge

Dated: NOV 18 1982

JUDGMENT — ORAL ARGUMENT

United States Court of Appeals

For the Seventh Circuit
Chicago, Illinois 60604

September 21, 1988

Before

Hon. WILLIAM J. BAUER, Chief Judge

Hon. WALTER J. CUMMINGS, Circuit Judge

Hon. RICHARD D. CUDAHY, Circuit Judge

Nos. 87-2548, 87-2609 and 87-2622

CHARLES W. LEIGH &
ERVIN F. DUSEK,
Plaintiffs-Appellants,

and

ESTATE OF GEORGE
JOHNSON, et al.,
Intervening Plaintiffs-Appellants,
Cross-Appellees,

vs.

CLYDE WILLIAM ENGLE, et al.,
Defendants-Appellees,
Cross-Appellants.

Appeals from the United States District Court for the Northern District of Illinois, Eastern Division.

No. 78-C-3799
BRIAN BARNETT DUFF,
Judge.

This cause was heard on the record from the United States District Court for the Northern District of Illinois Eastern Division, and was argued by counsel.

On consideration whereof, IT IS ORDERED AND ADJUDGED by this Court that the judgment of the said District Court in this cause appealed from be, and the same is hereby, AFFIRMED, with costs, in accordance with the opinion of this Court filed this date.

(3)

No. 88-1066

Supreme Court, U.S.
FILED
JAN 20 1989
JOSEPH F. SPANIOL, JR.
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1988

ESTATE OF GEORGE JOHNSON, ELEANOR MADSEN, CARMEN COLON, CASIMIRA MACIAS, SOLEDAD FREGOSO, MANUEL COLON, HILDA VALDES, CARMEN REGALADO, AMERICA SUAREZ, FERDINAND KANGISER, MARIA ROMERO, RAFAEL MENDOZA, JOSE LUIZ CORONA, HERIBERTO PIZZARO, RAMON GONZALAS, AND GUILLERMINA OLIVARES, for themselves and all participants in the Reliable Profit Sharing Plan Trust except CHARLES W. LEIGH AND ERVIN F. DUSEK, the Plaintiffs,

Petitioners,

v.

CLYDE WILLIAM ENGLE, NATHAN DARDICK, RONALD ZUCKERMAN, LIBCO CORPORATION, TELCO MARKETING SERVICES, INC., TELVEST, INC., THE RELIABLE EMPLOYEES' PROFIT SHARING PLAN TRUST, AND NATIONAL BOULEVARD BANK OF CHICAGO, a National Banking Association,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Seventh Circuit

BRIEF IN OPPOSITION OF RESPONDENTS NATHAN H DARDICK, RONALD K. ZUCKERMAN AND NATIONAL BOULEVARD BANK

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20pp

QUESTION PRESENTED FOR REVIEW*

Whether the Court of Appeals for the Seventh Circuit erred in holding that the District Court was not clearly erroneous in finding that although respondents breached a fiduciary duty owed to a profit sharing plan, they obtained no personal profits through the use of the assets of the profit sharing plan.

* Respondents Nathan H Dardick and Ronald K. Zuckerman are individuals. Respondent National Boulevard Bank is a wholly-owned subsidiary of Boulevard Bancorp, Inc.

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No. 88-1066

IN THE

Supreme Court of the United States

OCTOBER TERM, 1988

ESTATE OF GEORGE JOHNSON, ELEANOR MADSEN, CARMEN COLON, CASIMIRA MACIAS, SOLEDAD FREGOSO, MANUEL COLON, HILDA VALDES, CARMEN REGALADO, AMERICA SUAREZ, FERDINAND KANGISER, MARIA ROMERO, RAFAEL MENDOZA, JOSE LUIZ CORONA, HERIBERTO PIZZARO, RAMON GONZALAS, AND GUILLERMINA OLIVARES, for themselves and all participants in the Reliable Profit Sharing Plan Trust except CHARLES W. LEIGH AND ERVIN F. DUSEK, the Plaintiffs,

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v.

CLYDE WILLIAM ENGLE, NATHAN DARDICK, RONALD ZUCKERMAN, LIBCO CORPORATION, TELCO MARKETING SERVICES, INC., TELVEST, INC., THE RELIABLE EMPLOYEES' PROFIT SHARING PLAN TRUST, AND NATIONAL BOULEVARD BANK OF CHICAGO, a National Banking Association,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Seventh Circuit

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BRIEF IN OPPOSITION OF RESPONDENTS NATHAN H DARDICK, RONALD K. ZUCKERMAN AND NATIONAL BOULEVARD BANK

OPINIONS BELOW

The opinion of the Court of Appeals for the Seventh Circuit for which the petition is sought is reported at *Leigh v. Engle*, 858 F.2d 361 (7th Cir. 1988). The findings of fact and conclusions of law of the District Court for the Northern District of Illinois are reported at 669 F. Supp. 1390 (N.D.Ill. 1987). A Memorandum and Order of the District Court for the Northern District of Illinois is reported at 619 F. Supp. 154 (N.D.Ill. 1985). The first opinion of the Court of Appeals for the Seventh Circuit is reported at 727 F.2d 113 (7th Cir. 1984) ("Leigh I").

STATEMENT OF THE CASE

A. The Parties.

Petitioners are all former employees of Reliable Manufacturing Company ("Reliable") and beneficiaries of the Reliable Employees' Profit Sharing Plan (the "Plan"). Petitioners intervened in a suit originally brought by the former owners of Reliable for the alleged wrongful investment of Plan assets under the Employee Retirement Income Security Act of 1974 ("ERISA").

Respondent Clyde W. Engle is an officer, director and part-owner of respondent Libco Corporation, which purchased Reliable in 1977. Respondents Nathan H Dardick and Ronald K. Zuckerman became administrators of the Plan on September 15, 1977. The National Boulevard Bank became trustee of the Plan in February 1979, after

the present lawsuit was originally filed, and thus was not a party to that lawsuit. After petitioners intervened, they joined in plaintiffs' original wrongful investment claim and added a second claim, for wrongful distribution of Trust assets, in which they named the original defendants and added the Bank as a defendant for that claim alone. The Seventh Circuit found in favor of the Bank on that claim in all respects and petitioners do not seek review of any aspect of the Court's ruling on that claim. Thus, the Bank is not properly a respondent here.

B. The Challenged Investments.

After becoming Plan Administrators and assuming responsibility for Plan assets, Dardick and Zuckerman, upon advice of counsel, decided to diversify the investment of Plan assets and sought advice from a financial analyst. The analyst recommended the common stock of Berkeley Bio-Medical, Inc. ("Berkeley"), Outdoor Sports Industries ("OSI") and Hickory Furniture Company ("Hickory"). Dardick and Zuckerman kept approximately 70 percent of Plan assets in short-term debt instruments and invested the remainder of the assets in the stock of the three companies. The Trust's total investment in Berkeley was $71,580.53; in OSI, $77,736.83; and in Hickory, $72,433.21.

Following independent consultation with the same investment advisor and personal study of the three companies, Engle concluded that each of the three companies were sound and prudent investments, and Engle and related entities began investing in Berkeley, Hickory and OSI. During this time-period, the first half of 1978, Libco had assets of approximately $48 million and a steady cash flow from operating subsidiaries and liquidation of its lease portfolio, Engle had a personal net worth of almost $5

million, and a Libco subsidiary, Telco Marketing Services, had refinanced a bank loan and obtained $1.78 million for use in investments.

1. Berkeley

As to Berkeley, the Trust purchased for $71,580.53, a total of 15,800 shares of stock, constituting .65 percent of the outstanding Berkeley shares. Engle and related entities, not including the Trust, purchased more than 10 percent of the outstanding Berkeley shares. When Engle and related entities filed a Schedule 13D on their Berkeley holdings, they did not identify the Trust as a reporting person, but included the Trust's shares in calculating the shares controlled, thereby forcing an earlier public disclosure of their holdings than would otherwise have been necessary.

Engle became involved in a control contest for Berkeley, which was settled when Engle and related entities agreed to sell their stock at a substantial premium. The Trust was not a part of the original settlement until Dardick insisted that the Trust's shares be bought back at the same price, thereby providing the Trust with a substantial benefit. The Trust enjoyed a profit of $118,500, or 66 percent from the sale of its Berkeley stock.

2. OSI

In the OSI situation, the Trust purchased for $77,736.83 a total of 12,500 shares of stock, constituting .87 percent of the outstanding OSI stock. Engle and related entities, not including the Trust, purchased almost 21 percent of the outstanding OSI stock. The Schedule 13D filed by these entities disclaimed any interest in the Trust assets

but included the Trust shares with those reported and thus again caused an earlier disclosure of the stock holdings of the Engle-related entities than would otherwise have been required.

Although the Engle-related entities were involved in a control contest for OSI, the contest ended when a white knight entered and made a tender offer for all outstanding OSI shares. The Trust tendered its OSI shares and enjoyed a 141 percent profit of $109,763.17.

3. Hickory

As to Hickory, the Trust purchased for $72,433.21 12,000 shares of stock, constituting .67 percent of the shares outstanding. Engle-related entities conducted a control contest for Hickory, and eventually succeeded in gaining majority ownership of the company. Their Schedule 13D again disclaimed any beneficial interest in Trust assets, but again disclosed the Trust's shares. The Trust sold its OSI stock for a 4 percent profit of $2,566.79.

Thus, in little more than one year, the Trust's investments in Berkeley, Hickory and OSI together produced profits for the Trust of $159,249.43, for an overall return on investment of 72 percent. All of these profits were realized by the Trust alone. Respondent Dardick made no personal investment in the stock of Berkeley, OSI or Hickory during the relevant time period and thus enjoyed no profits from those stocks. Respondent Zuckerman's personal investment in the three companies was limited to 1,200 shares of Berkeley stock which he sold for a profit of $3,300.

C. Proceedings Below.

This case was originally tried in 1982 before United States District Court Judge George N. Leighton of the Northern District of Illinois, who entered judgment for defendants in all respects. *Leigh v. Engle*, slip op., No. 78 C 3799 (Nov. 18, 1982). On appeal, the United States Court of Appeals for the Seventh Circuit vacated the judgment and remanded for further proceedings. *Leigh v. Engle*, 727 F.2d 113 (7th Cir. 1984).

The Seventh Circuit reversed Judge Leighton's findings that Dardick and Zuckerman did not breach their fiduciary duties in investing Trust assets in Berkeley, OSI and Hickory, and held that Dardick and Zuckerman breached their fiduciary duties because they invested Trust assets where a potential conflict of interest existed.[1]

The Seventh Circuit ordered the District Court to find "an appropriate measure of damages, if any, with regard to all defendants found to be liable as fiduciaries." 727 F.2d at 137. The Court noted that the case presented "an extraordinarily difficult damages issue" because it required the District Court to determine whether the profits, if any, made by each breaching fiduciary were attributable to its own legitimate efforts or were attributable, in whole or in part, to the use of Trust assets. 727 F.2d at 137-38. The Court analogized the resolution of the causation issue in this ERISA context to resolution of similar

[1] The Seventh Circuit also held that respondents Engle and Libco were fiduciaries with respect to the selection, retention and supervision of Plan administrators and remanded for determination of whether they breached those fiduciary duties. The Seventh Circuit also vacated Judge Leighton's findings regarding the alleged delay in distribution of Trust assets, an issue not before the Court on this petition.

damages causation questions, such as where a copyright infringer has realized profits from both his own efforts and from his infringement, or where Trust assets have been commingled. The Court placed the burden on the breaching fiduciaries to show which profits were attributable to their own investments, apart from use or control of Trust assets, and required that all reasonable doubts be resolved in favor of the Trust beneficiaries. Petitioners never sought certiorari from this Court for the Seventh Circuit's damage theory formulation in *Leigh I*.

After retrial in 1986, District Court Judge Brian Barnett Duff entered his findings of fact and conclusions of law on August 27, 1987. 669 F. Supp. 1390 (N.D.Ill. 1987). In determining the appropriate measure of damages arising from the wrongful investment of Trust assets, Judge Duff found that the Trust suffered an opportunity loss of $6,704 from its investment in Hickory. The court found that respondents did not realize any profits from the investment of Trust assets in Berkeley, Hickory and OSI. The court found defendants did not need the Trust assets to enhance their own investments, and that the Trust investments did not affect the price of Berkeley, OSI or Hickory stock, did not allow defendants to prolong the secrecy of their acquisition programs, and did not affect the decisions of the other companies involved in the control contests to purchase stock held by Engle-related companies.

On appeal, the Seventh Circuit affirmed the District Court's findings and conclusions in all respects. Again terming the damage calculation a "formidable task", the Seventh Circuit noted that "the District Court did an admirable job with it." The Seventh Circuit again rejected petitioners' claim that they were entitled to all profits of Engle and related entities on their investments in Berkeley, OSI, and Hickory, and affirmed the trial court's finding

that respondents proved that any profits they realized on these investments were obtained through their own efforts and not through use of Trust assets. The Seventh Circuit also found not clearly erroneous the District Court's finding that petitioners suffered $6,704 in damages from the Trust investment in Hickory since the Hickory investment did not produce as high a return as more appropriate investment vehicles.

Petitioners filed the present petition for a writ of certiorari on December 20, 1988.

REASONS FOR DENYING THE WRIT

The Petition for a Writ of Certiorari should be denied because the decision of the Court of Appeals for the Seventh Circuit applied the correct legal standard and was correctly decided. The decision does not conflict with any prior decision of this Court or any federal appellate court. The Seventh Circuit decision did not involve an important question of federal law, but rather involved simply a holding that the trial court was not clearly erroneous in its factual findings that respondents obtained no personal profits through the use of Trust assets.

I.

THE COURT USED THE APPROPRIATE DISGORGEMENT ANALYSIS IN FINDING NO PROFITS WERE OBTAINED THROUGH USE OF TRUST ASSETS.

Section 1109(a) of ERISA provides that a breaching fiduciary must "restore to such Plan any profits of such fiduciary which have been made through use of assets of

the Plan by the fiduciary." 29 U.S.C. § 1109(a). In *Leigh I*, the Seventh Circuit held that the burden was on defendants found to have breached their fiduciary duties to show which profits, if any, were attributable to their own investments apart from control of the Trust assets. 727 F.2d at 138. The Seventh Circuit "read section 1109(a), providing that the fiduciary 'shall be subject to such other equitable or remedial relief as the court may deem appropriate,' as authorizing us to cast the burden of proof on the defendants here to insure that the disgorgement remedy is effective." 727 F.2d at 139. On that basis, the Seventh Circuit remanded to the District Court for determination of which of defendants' profits, if any, were made through use of Trust assets. Petitioners never sought relief in this Court from the Seventh Circuit's damages guidelines.

On remand, the District Court followed those guidelines and found that respondents made no profits through the use of Trust assets. 669 F. Supp. at 1401, 1403, 1404. On appeal, the Seventh Circuit found that the District Court did an "admirable job" with the "formidable task" of damages calculation, and affirmed. 858 F.2d at 366. The Seventh Circuit noted that "[i]n order to avoid disgorgement of part of its profits, the Engle group had to show that they did not result from misuse of trust assets. Judge Duff correctly held that defendants met this burden." 858 F.2d at 366.

The Seventh Circuit advanced five theories that potentially might have provided a causal connection between the use of Plan assets and the profits made by the Engle entities on the investment of their own assets. First, the Engle entities could have hidden stock from disclosure requirements by buying it with Trust assets. Second, the Trust assets could have provided the Engle entities with

otherwise unavailable capital. Third, the Trust's stock holdings could have enhanced the influence of Engle in control contests. Fourth, the Trust's holdings could have undermined settlement of the control contests. Finally, the Trust's purchases could have affected the market price of stock. However, after analyzing each of the five theories, the District Court found, and the Seventh Circuit affirmed, that on each, respondents had satisfied their burden of proving no causal connection. *See* 858 F.2d at 366-67.

Notwithstanding the thorough fact-finding and careful analysis on the causation issue, petitioners object because the result is to deny petitioners recovery of all of the profits realized by Engle and related entities through their separate investments in Berkeley, OSI and Hickory. Throughout this litigation, petitioners have repeatedly sought to obtain all profits earned by Engle and related entities but have been repeatedly rebuffed and criticized for their overreaching. *See, e.g.*, 858 F.2d at 366; 727 F.2d at 137. Petitioners persist, however, because of a misguided notion that once a prohibited transaction has been found, all profits of the fiduciary must be paid to the beneficiaries, regardless whether there is any causal connection between the breach and the profits, if any.

Petitioners' argument effectively eliminates the causation requirement from the remedial provisions of section 1109(a). *Cf. Brandt v. Grounds*, 687 F.2d 895, 898 (7th Cir. 1982) ("causal connection is required between the breach of fiduciary duty and the losses incurred by the plan"); *Chambers v. Kaleidoscope, Inc. Profit Sharing Plan and Trust*, 650 F. Supp. 359, 378 (N.D. Ga. 1986) (awards damages causally related to breach). Because they thoroughly misread the statutory language and misrepresent the Seventh Circuit's opinion, petitioners argue that

that decision allows a breaching fiduciary to keep illegal profits and that a plan has no remedy against a breaching fiduciary and his illegal profits unless the plan has suffered a loss from the breach. Petitioners' arguments are plainly incorrect, and are thoroughly discredited by the Seventh Circuit's straightforward application of the remedial scheme of section 1109(a). The Seventh Circuit decision is correct and need not be disturbed.

II.

THE SEVENTH CIRCUIT'S DECISION DOES NOT CONFLICT WITH ANY DECISIONS OF THIS COURT.

Petitioners claim that the Seventh Circuit decision is "probably in conflict with existing applicable decisions of this Court," but manage to set up conflicts with other cases only by misrepresenting the Seventh Circuit's decision. The Seventh Circuit's decision was legally correct and consistent with principles of ERISA and trust law upon which ERISA is based. Although it broke no new legal ground, the decision is wholly consistent with prior decisions of this Court and other federal courts in this area.

Under traditional trust law, a trustee is "liable for any profit he has made through the breach of trust, even though the trust suffered no loss." Bogert on Trusts, § 701, p. 206 (rev. 2d ed. 1982). The same principle is contained in ERISA section 1109(a) and was recognized throughout the Seventh Circuit opinion. No disgorgement was required by the Seventh Circuit, however, because the Court found that no one made any profit "through the breach of trust." Petitioners may deny the result of the fact finding, but application of the legal principle is unassailable.

Because petitioners misconstrue the facts here, they fail to recognize the distinctions between the present case and those cases with which they claim it conflicts. In both *Mosser v. Darrow*, 341 U.S. 267 (1951) and *Magruder v. Drury*, 235 U.S. 106 (1914), the trustee was surcharged because he allowed a third party to take for itself part of the profit rightfully belonging to the trust. In the present case, the lower courts stood ready to do likewise but after careful scrutiny determined that no one obtained a personal profit through use of trust assets. Similarly, with numerous other of petitioners' statements of general principles of trust law, the principles remain applicable, but stand in harmony with the Seventh Circuit opinion.

Petitioners disingenuously cite *Massachusetts Mutual Life Insurance Co. v. Russell*, 473 U.S. 134 (1985) and argue that the present case somehow presents a question left open by that decision. In *Massachusetts Mutual*, this Court held that section 1109(a) did not provide a cause of action for extracontractual or punitive damages to a beneficiary caused by improper processing of benefit claims. Petitioners claim that *Massachusetts Mutual* left open the question whether disgorgement of profits is available as "other equitable or remedial relief" under section 1109(a). In fact, disgorgement of "profits of such fiduciary made through use of assets of the plan by the fiduciary" is expressly provided for in section 1109(a), and was the remedy the Seventh Circuit analyzed and stood ready to apply in its opinion. The Court declined to order the disgorgement remedy here not because of any legal uncertainty or error, but because every federal judge that analyzed the facts determined that there was no causation between the breach by respondents and profits enjoyed by respondents as a result of their own investments and efforts.

The decision below is correct and consistent with prior law.

III.

PETITIONERS ARE EFFECTIVELY SEEKING REVIEW OF THE SEVENTH CIRCUIT OPINION IN *LEIGH I* AND ARE BARRED FROM DOING SO.

Petitioner claims that the Seventh Circuit's analysis was legally incorrect because it relied on a causation standard announced in *Leigh I* analogizing ERISA damages to apportionment of a copyright infringer's profits. In challenging this damages formulation, petitioners effectively ask this Court to rule as legally incorrect not the Seventh Circuit's decision in *Leigh II*, but rather the decision in *Leigh I*, 727 F.2d 113 (7th Cir. 1984). In *Leigh I*, the Seventh Circuit analogized to the copyright area in setting forth the causation guidelines for determining whether the profits of a breaching fiduciary are attributable, in whole or in part, to the use of the Trust assets. In *Leigh II*, the Seventh Circuit merely reviewed the District Court's fact findings on remand to determine if the court properly analyzed those causation guidelines. Petitioners here reject the notion that causation is even an issue once a prohibited transaction is found, and thus ignore the individual findings of *Leigh II*. Petitioners' challenge here is to the underlying causation guidelines enunciated by the court in *Leigh I*. Because the time to challenge *Leigh I* has long since expired, petitioners' request for review of that opinion should be here denied.

CONCLUSION

The Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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Dated: January 20, 1989

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(4)

No. 88-1066

Supreme Court, U.S.
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JOSEPH F. SPANIOL, JR.
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In The
Supreme Court of The United States
October Term 1988

ESTATE OF GEORGE JOHNSON, ELEANOR MADSEN, CARMEN COLON, CASIMIRA MACIAS, SOLEDAD FREGOSO, MANUEL COLON, HILDA VALDES, CARMEN REGALADO, AMERICA SUAREZ, FERDINAND KANGISER, MARIA ROMERO, RAFAEL MENDOZA, JOSE LUIZ CORONA, HERIBERTO PIZZARO, RAMON GONZALAS, AND GUILLERMINA OLIVARES,
For Themselves and all Participants in the Reliable Profit Sharing Plan Trust except CHARLES W. LEIGH AND ERVIN F. DUSEK, the Plaintiffs.

Petitioners

v.

CLYDE WILLIAM ENGLE, NATHAN DARDICK, RONALD ZUCKERMAN, LIBCO CORPORATION, TELCO MARKETING SERVICES, INC., TELVEST, INC., THE RELIABLE EMPLOYEES' PROFIT SHARING PLAN TRUST, AND NATIONAL BOULEVARD BANK OF CHICAGO, A National Banking Association.

Respondents

On Petition For A Writ Of
Certiorari To The United States Court Of
Appeals For The Seventh Circuit

PETITIONERS' REPLY MEMORANDUM

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February 17, 1989

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5p

No. 88-1066

In The
Supreme Court of The United States
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ESTATE OF GEORGE JOHNSON, ELEANOR MADSEN, CARMEN COLON, CASIMIRA MACIAS, SOLEDAD FREGOSO, MANUEL COLON, HILDA VALDES, CARMEN REGALADO, AMERICA SUAREZ, FERDINAND KANGISER, MARIA ROMERO, RAFAEL MENDOZA, JOSE LUIZ CORONA, HERIBERTO PIZZARO, RAMON GONZALAS, AND GUILLERMINA OLIVARES,
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PETITIONERS' REPLY MEMORANDUM

I.

Pursuant to Rule 22.6, Petitioners call the attention of this Court to the recent decision by the Ninth Circuit Court of Appeals in *Amalgamated Clothing & Textile Workers Union v. Murdock, 861 F.2d 1406* (1988) in support of their argument in the first

full paragraph at page 14 of the petition, that the lower court's decision is likely to create conflict among the circuits.

II.

Pursuant to Rule 22.5, petitioners make the following reply. CLYDE WILLIAM ENGLE, LIBCO CORPORATION, TELCO MARKETING SERVICES, INC., TELVEST INC., AND THE RELIABLE EMPLOYEES' PROFIT SHARING PLAN TRUST, certain named Respondents, filed no Brief in Opposition. CLYDE WILLIAM ENGLE, and LIBCO CORPORATION, though did cross petition this Court, in Docket No. 88–1232, presenting questions challenging their liability and the lower court's method of determining damages under ERISA. That cross petition does not address the question presented by petitioners and requires no reply.

Respondents, NATHAN DARDICK, RONALD ZUCKERMAN, and NATIONAL BOULEVARD BANK claim to oppose the granting of a Writ of Certiorari to petitioners; but, do so only by restating the QUESTION PRESENTED by petitioners in a manner that lacks "sufficient general importance." See *United States v. Nobles, 422 U.S. 225, 241-242 n. 16 (1975).*

This attempt of certain respondents to oppose the issuance of a Writ of Certiorari to the lower court, by restating the QUESTION PRESENTED bares the serious flaw in its opposition to disgorgement under the common law. The "appropriate disgorgement analysis" urged in support of the lower court's decision confuses the restitutionary remedy under 29 U.S.C. Section 1109 with the common law remedy of disgorgement intended to be a deterrent to breach of the duty of loyalty.

The principal object of the restitutionary remedy expressed in 29 U.S.C. Section 1109 is the apportionment of the wrongdoers' gain and its restitution to the beneficiary along with any losses that may have been incurred. The principal object of the common law remedy of disgorgement also expressed in 29 U.S.C. Section 1109 is preventive. Bogert, *Trusts and Trustees*, Section 543 at page 480 (2d ed. 1960). See also, *Restatement of the Law of Trusts 2d.* Section 206j (1959). There is no punitive remedy expressed

in 29 U.S.C. Section 1109 because the deterrent aspect of disgorgement serves that purpose.

By their misplaced concern that petitioners would obtain all respondents' profits, i.e. a "windfall", these respondents claim that *the disgorgement remedy must be made effective*, as the lower court held, by requiring the Northern District of Illinois to read into 29 U.S.C. Section 1109, a "hybrid" remedy that confuses restitution and disgorgement; and, that hinges upon a "factual causation" which ignores the legislative history of ERISA relied upon by this Court in *Massachusetts Mutual Life Insurance Company v. Russell, 473 U.S. 134, 105 S.Ct. 3085, 87 L.Ed 2d 96 (1985) fn 12.*

The facutal analysis and burden of proof relied upon by these respondents in support of the lower court is misdirected given the findings in Leigh I that respondents engaged in prohibited transactions. Had respondents lost both their investment *and the invested trust assets*, restitution of the trust assets would be required. However, where as here, respondents profited by the use of trust assets and gained 9.8 million dollars, returning the trust assets with a 72% return and retaining 9.8 million dollars of profit, is not an "appropriate disgorgement analysis." The finding of prohibited transactions is the misuse and mismanagement of plan assets that ERISA was designed to prevent. Section 1109 does not suggest that a further apportionment of profits or "factual causation" prior to disgorgement is intended. Disgorgement of profits made as a result of a violation of ERISA's fiduciary provisions is the only proper remedy given the misuse and mismanagement of the plan's assets by these respondents.

Respondents also oppose a Writ of Certiorari because the lower court *recognized* traditional trust law principles. The petitioners' reasons in seeking a Writ of Certiorari lay claim to the lower court's failure to apply traditional trust law principles. Traditional trust law principles do not mix the remedies of restitution of losses and disgorgement of profit. The Department of Labor expressing its views in Leigh I, and citing Bogert, *Trusts and Trustees* Section 543 at p. 480 (2d ed. 1960) and *Restatement of the Law of Trusts 2d.* Section 206j (1959), concluded that disgorgement of profits is a proper remedy under these circumstances. In doing so, it stated that disgorgement under the

common law is not a restitutionary remedy--it is intended to be a deterrent to breach of the duty of loyalty. Leigh I, Record, Amicus Brief of Department of Labor, pages 25-28. It is the erroneous engrafting of "factual causation" and "the apportionment of profits" from the remedy of restitution onto the traditional trust law remedy of disgorgement that allows respondents to engage in prohibited transaction and to retain 9.8 million dollars of profit in this case.

Respondents finally oppose a Writ of Certiorari because petitioners' challenge is to the underlying causation guidelines enunciated in Leigh I. A premature review of Leigh I by this Court prior to the Northern District of Illinois decision and the lower court's affirmance relying upon Leigh I, was avoided in order that the question presented might be fully developed for this Court's consideration.

The importance and substantiality of the QUESTION PRESENTED by petitioners is not denied by these respondents. Their only opposition arises from their restating the QUESTION PRESENTED in order to argue that the traditional trust law remedy of disgorgement is not effective until and unless the restitutionary remedy is engrafted thereon. 29 U.S.C. Section 1109 remedy of disgorgement reflects the crucible of congressional concern that fiduciaries would misuse and mismanage trust assets. Disgorgement requires no weakening by diluting it with the restitutionary remedy.

In light of respondents' refusal to face the issues presented in the petition by restating the QUESTION PRESENTED, the need for plenary review of the decision of the lower court is now indisputable. Petitioners suggest that summary reversal may be in order given the recent decision by the Ninth Circuit in *Amalgamated Clothing & Textile Workers Union v. Murdock, 861 F.2d 1406 (1988).*

Respectfully submitted,

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